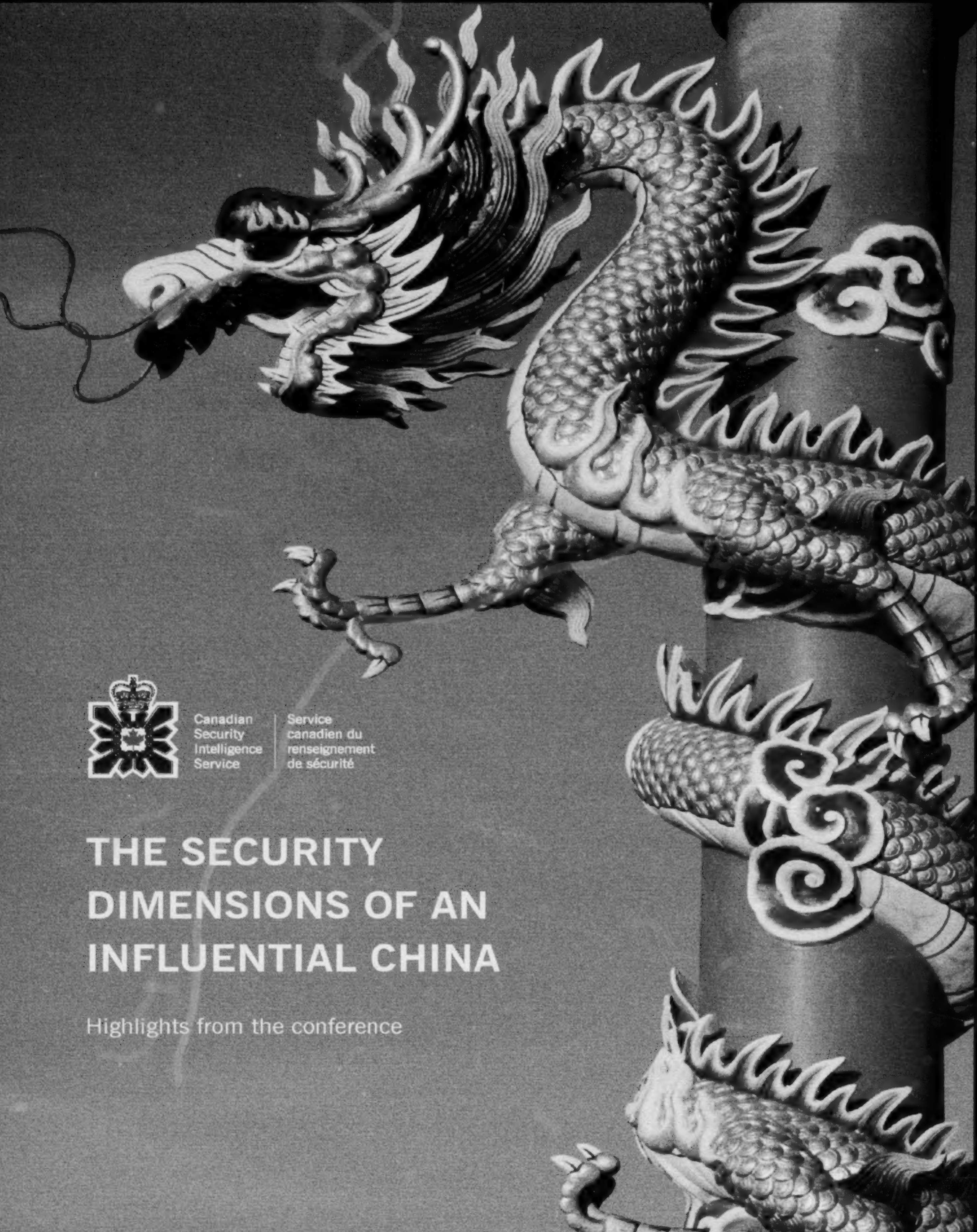

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THE SECURITY DIMENSIONS OF AN INFLUENTIAL CHINA

Highlights from the conference

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This report is based on the views expressed during, and short papers contributed by speakers at, a conference organised by the Canadian Security Intelligence Service as part of its academic outreach program. Offered as a means to support ongoing discussion, the report does not constitute an analytical document, nor does it represent any formal position of the organisations involved. The conference was conducted under the Chatham House Rule; therefore no attributions area made and the identity of speakers and participants is not disclosed.

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THE SECURITY DIMENSIONS OF AN INFLUENTIAL CHINA

A conference of the Canadian Security Intelligence Service (CSIS)
held in collaboration with National Defense Canada

Highlights from the conference
28 February - 1 March, 2013, Ottawa

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The conference and its objectives

On 28 February and 1 March 2013 and in partnership with National Defence Canada, the Canadian Security Intelligence Service (CSIS) hosted a two-day conference on China as part of its Academic Outreach program. Conducted under Chatham House rule, the conference provided an opportunity for the presenting specialists and other participants to examine the consequences for national and international security of China's newly-gained global influence.

The papers contained in this conference report reflect the views of the independent scholars and analysts who presented them, not those of CSIS. The Academic Outreach program at CSIS, established in 2008, aims to promote a dialogue between intelligence practitioners and outside experts from a variety of disciplines and cultural backgrounds working in universities, think tanks and other research institutions in Canada and abroad. It may be that some of our academic interlocutors hold ideas or promote findings that conflict with our own views and analysis, yet it is for this reason that there is value in the conversation.

The China conference welcomed an impressive roster of researchers from Canada, Europe, Asia and the United States. As with most Academic Outreach events there was a diversity of expert opinion on the floor, but as to the central premise of the gathering there was consensus, namely, that the economic and political rise of China is ushering in a new period of geopolitics, representing an important moment not just for China but for many other countries as well.

Political Trends Arising from the 18th Congress of the Chinese Communist Party

Are we witnessing the beginning of a new political era in China? The year 2012 was indeed China's equivalent of an electoral year, with factions and individuals jockeying for positions in the succession race. The Bo Xilai case, when it exploded onto the scene, provided unparalleled insight into the competition at the top; it also increased the stakes for those who wanted to gain some advantage from it and those who wanted to contain its impact. This window has now closed as we settle into the post-succession situation and political actors are aware that much more can be lost than gained through overt campaigning at this point.

It is useful to contrast societal analyses of China, which usually emphasise bottom-up changes, with the country's actual political life, in which factional and personal ties at the top matter greatly. After the events of Tiananmen Square in 1989, ideological and political conflict were largely contained, or at least hard to uncover, because Deng Xiaoping and his successors enforced a policy of "core leadership" dominance over factions and considerably improved the protection of "state secrets". Since 2010, however, we have seen an apparent return to factional jockeying that suggests stark political differences. Cynicism may also prevail amongst the public about the personal priorities of top leaders, yet the Party, without a clear electoral process, has thanks to its debates revived a form of political life in China.

The growing use of social media creates unexpected outburst of public discontent, but these often look in retrospect as brushfires: quickly started but just as quickly extinguished and forgotten. We may not understand the ramifications of feuds at the highest echelons of China's leadership, but for the past two years we have nonetheless been able to observe ongoing divergences in policy-making. It remains hard to conceive that more than half of the country's fate is decided by 25 senior figures, or perhaps even fewer. However, it is true.

The period from 2010 to 2012 witnessed a resurgence of factional conflict along familiar, pre-1989 political lines: the rule of law and the constitution v. the Party and security organs; assertive nationalism v. rule-based integration; and dominant state-owned enterprises (SOEs) and special interests v. more dispersed advocates of a new wave of economic reforms. It may be true that political leaders actually relate to each other across some of these dividing lines even if political boundaries are clearly drawn, or inferred, by China's media and public intellectuals. In contrast, analysts have often given more weight to the importance of bureaucratic fragmentation and competition amongst organisations to explain the nature of Chinese policy-making. One assessment of the legacy of the former leaders, Hu Jintao and Wen Jiabao, is that their indecisiveness and ambiguity encouraged such fragmentation and competition.

In this context, the 18th Party Congress, held in November 2012, appeared like a winner-takes-all game. However, we know this cannot be entirely the case because the Politburo is more evenly distributed than its Standing Committee and support from former president Jiang Zemin's base, very prominent in the succession, is unclear and may at best make Xi Jinping beholden to it. Party elders dominated the decision-making process—a broadened politburo meeting—and were well served by the propaganda value of official videos of the Party Congress. If they were not demoted, those leaders who were thought to be closer to Hu Jintao and favour reform did not gain prominence. Wang Qishan is the exception, although he was shifted to head the Party's Discipline and Inspection Commission, away from economic affairs. The failure of Zhou Xiaochuan, the head of the central bank, to be re-elected to the Central Committee also seemed like a choice against reform, even though it was counter-balanced by the fact that Chen Deming, China's conservative minister of Commerce was not re-appointed.

Xi Jinping's ascent in this troubled environment wipes the slate clean. Not only does he present a "personal" style, contrary to Hu's "harmonious" but gray approach to power; he also plays openly on conservative instincts, frequently quoting Mao and an (officially unpublished) assessment in which the first thirty years of the PRC are seen to be as relevant as the latter period. Xi extols the virtues of the military and plays up tensions with Japan over the Senkaku/Diaoyu Islands, although this may also be the result of more rational calculations to contain potential incidents to one area of Asia. On these issues, Xi's long-standing and diverse associations with the military are clear.

Xi parted ways formally with Bo Xilai, which has allowed his supporters to take swipes at reformers for their lack of concrete actions. It is likely that the way in which the Bo Xilai case unfolded played a significant role in top-level disputes and that its resolution influenced in large part the results of the succession process: Bo's trial and the Party Congress were announced simultaneously, and Xi Jinping accepted a few losses amongst his harder-line military followers (like General Liu Yuan, who was not promoted) in order to secure his overall victory and to lash out more freely at the more liberal factions. He downplays reform as an ongoing process, describing it as a permanent quest for improvements rather than an epoch-making change. His anti-corruption drive, led from above by Party organs and laced with attacks on private lives, hangs a sword over many of the regime's senior figures.

Various debates that raged before November 2012—eg. the importance of constitutionalism or whether references to "special interests" were veiled attempts at criticising SOEs' influence—have disappeared from the public's view. The 2013 Chinese New Year incident caused by a censored editorial in the *Nanfang Zhoumou* happened because editors there used Xi's new catch word about the "Chinese dream" to promote constitutionalism; this was considered unacceptable and promptly removed. We could also note at that time that protests against Japanese interests, when the Senkaku/Diaoyu tensions reached their peak, also disappeared from sight. It is nearly impossible to argue that the confrontations in the East and South China Sea were due to competition and overlapping lines of command amongst administrations. Xi Jinping's arrival in power coincides with a clamp-down at the top and much less space for public Party debates. In his unofficial remarks while in Shenzhen, Xi actually expounded on "the Party as the core", setting a higher standard for Party unity than previously. Hu Jintao's loss of visible influence has been stunning, with "harmony" for example disappearing overnight from the policy discourse. Hu's first public appearance after the 18th Party Congress was in Cunyi, to celebrate the Party conference that took place there at the beginning of the historical period known as the Long March: by becoming then the head of the Military Affairs Commission (MAC), Mao had effectively entrenched his power on the Party. In contrast, Hu's trip had all the appearances of a curtain call celebrating his successor, who was appointed head of the MAC even before the 18th Party Congress, a rare loss of face for an outgoing leader.

> *It is nearly impossible to argue that the confrontations in the East and South China Sea were due to competition and overlapping lines of command amongst administrations.*

Rather than the previous emphasis on collective leadership, we can anticipate a return to a more personal style of leadership. We may also assume that Xi Jinping wants freedom to move right *and* left on China's political spectrum, much as Mao did in his time. Lately, he has balanced his use of Mao's quotes with allusions to staid classical Chinese thinkers. Some of his points, particularly the restated significance of Party leadership, echo the former statesman Liu Shaoqi's concept of "new democracy". They are also reminiscent of a period of late Soviet history, after the Brezhnev era, when Yuri Andropov, a party stalwart with intelligence connections going back to the 1930s, tried Party-led modernisation without reforms. The uncertainty about Western economies, the impressive expansion of China's security apparatus and the stress on *weiwen*, or stability, certainly generate a comparable context for today's Chinese leaders. We may wish to remind ourselves that, under Andropov, the Soviets shot down a civilian Korean airliner that had diverted from its itinerary. The oft-discussed theme of the "red princes", the second and third generation children of successful revolutionaries, coincides with a renewed sense of legitimacy that Xi wishes to symbolise. The destinations he chose for his first foreign visits include South Africa and Russia, which Beijing sees as close partners. The move appears to be a perfect mirror to the US pivot to Asia, and to the recent European trend towards giving more importance to Asian partners other than China.

Rationalisation of state institutions is likely to happen under Xi, and he has not challenged the previous team's efforts to balance the economy towards domestic consumption and to increase social benefits. This is as much a leftist as a rightist theme. There has been mention of possible further reform addressing the "re-education through labour" system, which has already been scaled down in previous years. Xi emphasises austerity and simplicity, themes that cannot displease ordinary citizens, but whose implementation has to be monitored in the longer run.

Because foreign partners depend so much on China's continued path towards global integration, there has been speculation that Xi Jinping might be a "closeted reformer" and that he would launch a major second wave of economic reforms, even as he is less likely than his predecessor to promote political reform. The jury is still out. The incoming prime minister, Li Keqiang, has been remarkably absent from the limelight during that interval, but this may be one instance of formal respect for due process.

Xi, however, is not Mao. The shelf life of his Standing Committee is limited to five years by customary age limits (if they are respected), and his use of nationalist or populist arguments may inadvertently stir other social and political forms of protest in a deeply divided society. Observers have often been too optimistic in predicting change from below, based on economic currents and social media. There is a contradiction between China's need for more equity in development, reining in special interests, limiting corruption and firming the Party's grip on power. Paraphrasing the former US president Abraham Lincoln, we may say that Xi and the Party are likely to exercise complete authority for a short time, instilling fear amongst those who go astray, including within the state apparatus; but it will prove increasingly difficult, if not impossible, to maintain that level of control in the future.

Xi has given no sign that he is ready to introduce a separation of powers, a recurrent if somewhat abstract theme of political reformers inside the Party. He may compensate for this by introducing limited liberalisation and loosening the Party's grip on certain aspects of ordinary life. This would create a new cycle of *fang-shou*, "release and recontrol", management. However, the sophistication of China's economy and society now requires more formal rules to ensure the separation of public and private interests, not just liberalisation at the local level.

It is challenging to look five years ahead when a new leadership team will rise under Xi and Li. Jiang Zemin was an even more precarious successor in 1989, and yet his political influence is still felt today. With Xi, we have a leader who is strong-willed, immune from the typical doubts of the reformists and staunchly convinced of China's mandate to compete with the West. Those are undoubtedly the arguments on which he bases his legitimacy. It remains to be seen whether the increasing demands of the Chinese people will cloud his future.

Party Consensus and Communist Ideology After Bo Xilai

The CCP as an ideological nation

The Chinese Communist Party (CCP), with over 80 million members in 2012, is as large as many nation-states and certainly as well organised. Tracking its ideology and political consensus is akin to describing a national polity. The noted historian of Qing and Republican China, Philip Kuhn, summarised his analysis of ideological life in 18th-century China by observing that "Chinese culture was unified but not homogeneous"[1]. This observation applies to CCP ideology and political consensus: a shared ideology, Marxism-Leninism-Mao Zedong Thought, or Maoism—pervades the CCP, but that ideology is not experienced in the same ways in different domains of the Party—from the power elite with their official pronouncements, to the establishment elite with their practical duties, to lower and local levels of rank and file or intellectuals and specialists of lower Party rank with their fears. In short, we see the same words, but variant meanings across these domains of the CCP. The question of "party consensus" can be better understood in these terms.

At the official level of the *power elite*, Party consensus has been rocked by a major scandal: the Bo Xilai affair. Pre-dating that and continuing past it is the ongoing official contention between two models for Party leadership and development: the Chongqing and Guangdong models, captured in the phrase "how to cut up the cake, or how big to make the cake" (equity v. growth). At the level of the *establishment elite*, we see the return of the public intellectual using orthodox language to pursue variant ends, either supporting the development model or promoting further reform, or even reaction. Finally, at the lower or local levels there are two challenging ideological issues: nationalism and a crisis in morality. This has invited a broader range of pronouncements and suggestions from *non-elite Party members* ranging from neo-Maoism, to neo-Confucianism, to a sort of "liberation theology" populism, as well as a number of voices looking for a liberal, moderate and tolerant version of Party ideology, not unlike a novel form of the concept of "new democracy".

Official ideology and the politics of consensus

Xi Jiping has decided the way to save China is to save the CCP. All agree that his mandate is to combat corruption in order to ensure the survival and success of the CCP; the ideological debates and challenges to consensus happen within that mandate. Not saving the CCP is not a legitimate topic and is relegated to the domain of illegal expression. In this, Xi Jinping is modelling himself on the ideological helmsmanship of Deng Xiaoping, balancing different fractions, factions and preferences amongst the power elite. That it is hard to pin Xi to the Youth League faction or the Shanghai faction should be surprising in this sense. In addition, as others will point out, his top colleagues are not his personal choices but have been handed to him by his predecessors, Hu Jintao and Jiang Zemin; it will therefore take a year or two before he can possibly make his personal mark. This appears to be an intentionally conservative piece of statecraft in the CCP ruling system—as new general secretaries, from Deng Xiaoping to Zhao Ziyang to Jiang Zemin and Hu Jintao—faced a similar array and took up to five years to get their team into place and then do something new (consider Zhu Rongji in 1998). Clearly, this arrangement is intentional and it is inherently conservative, tying the hand of the new supreme leader and protecting against rash changes at the cost of making any change laborious. This is revolutionary administration with Qing characteristics!

The Bo Xilai case

As far as I can tell, the "Maoism"—red songs, rhetoric and imagery—of Bo Xilai's Chongqing experiment, was not fundamentally ideological but rather a crude piece of political populism. Bo was a successful, internationally-oriented reformer as Mayor of Dalian and his family, under patriarch Bo Yibo, was anything but radically Maoist. Bo's case is about power politics, and he lost. The Chongqing model as state-owned development is not discredited by his fall; it continues to stand as a test site, along with its alternative model, the state-led development model of Guangdong. The crisis of faith for the power elite in the Bo case is how to limit the privileges of the elite before they break the system or provoke massive public rejection. It is a crisis of legitimacy in a plutocracy.

Maoism is ill-suited to explain away these inequities, despite the power elite's attempts at doing so. Jiang Zemin's "Three Represents" give official licence to capitalists ("entrepreneurs") to join the Communist Party, prohibits class warfare (for "the benefit of the whole people") and explains why technical and educational elites should be privileged, ie. leading forces of science and culture. Hu Jintao's concepts of scientific development and harmonious society are corollaries of these axioms.

Establishment ideology and the politics of consensus

Ideology and political consensus in the massive establishment of the CCP administration is mostly about articulating and applying that orthodoxy. To many outsiders, not to mention non-Party Chinese students, constant references and elaborations of these top Party slogans is both vacuous and pathetic. In the establishment, however, these are the tools for political contention, and China's establishment intellectuals use them with skill. Policy terms come and go, but the shape of the ideology does not change so fast. The ideological consensus in the establishment is that the Party should, indeed, be in charge because the market is capricious and less educated people do not have the moral quality (*suzhi*) to make good decisions. Alexander Hamilton would understand.

The debate is over *how* and which Party members should be in charge in a given case. The struggle we have seen in recent months is between putting Party hierarchy in unquestioned charge or giving the relevant technical specialists (also Party members, of course) the free hand to choose. Two recent examples make this clear. The first is the public letter of Beida Law professor, Zhang Qianfan, signed by 70 noted Chinese intellectuals in December 2012. Cast in the tones of a petition, this public letter calls upon the CCP to implement more fully the rule of law already proclaimed in the Chinese constitution and related laws. Amongst the signatures is that of Zhang Lifang, a Beijing intellectual who also signed Charter 08. The contrast is telling: this letter does not call for multi-party democracy, yet it also calls the Party to task for failing to deliver on reform. While this seems milder than Charter 08, it is not without effect. The second example underscores that this cooperative approach from the establishment is anything but craven compliance. The *Southern Weekend* incident that blew up in January 2013 over censorship issues reflects a wide-spread sense of "I've had enough" amongst the professional Party establishment; heavy-handed censorship is getting push-back from inside the CCP. Amongst those protesting the arbitrary re-writing of the now notorious New Year's Day editorial for the paper, is the faculty of the Journalism Department at Nanjing University, hardly a hotbed of anti-regime activity. The consensus at the establishment level is that regularisation is needed, along with the predictability of sensibly adjudicated rules. This may not be democracy, but it is an ideology of relative political liberalism inside the CCP.

Non-elite ideology and the politics of consensus

Ideology and political consensus at the non-elite level are, of course, yet more diverse. Still, the Party establishment elite and power elite spend a lot of time trying to "read the tea leaves" of their grass-roots members as a way to gage the issues in Chinese society more broadly. What we see at this non-elite level is that a wide range of social interests and concerns can and do find expression in the language and political practise of Party orthodoxy. Using terms drawn from the harmonious society and scientific development worldview does not necessarily reflect passive subordination or cynical posturing. The ideology at the local level makes sense in terms of popular values and expectations about rulership. While these contrasting views often do not contend with, or even take note of, other views, they do reflect the vibrancy of political and intellectual life in the CCP that we might miss by focussing on the choreographed moves executed in Beijing's halls of power.

The variety of non-elite pronouncements reflects two primary realities of ideological life in the CCP: the pervasive power of nationalism and a broadly recognised crisis in morality. The internet is our easiest access to this non-elite world, though it includes non-Party as well as Party voices. Nationalism has been promoted by the CCP with particular gusto since the early 1990s as part of the anti-dote to the crisis in faith following the Tiananmen repression. In this case, propaganda worked. It built upon the central role of Chinese nationalism in Maoism; the story Mao told in 1940 *is the story* that Xi Jinping tells today: China was great, China was put down, China has risen again and will continue to rise. It is too much to say that the Senkaku/Diaoyu Islands stand-off is produced by this ideology, but it is certainly aided and abetted by it. Official nationalism is, however, a dangerous two-edged sword for the CCP as domestic protesters know very well to present their protests against local leaders or issues in terms of this sanctified nationalism. The second issue that echoes across the non-elite world of the Party is the recognition of a profound crisis in morality. This has brought renewed efforts at "revolutionary education", a commitment to the strictures of modern professional norms and even a turn to the "roots" of Chinese civilisation, a version of Confucian philosophy. The ideological consensus from the rank and file centres on the need to find a leader, a concrete ideology or a group in which *a sensible person can actually believe*. Trust is at an all-time low. China may well have reached the ideological stage of the USSR and Eastern Europe in the 1980s: nobody believes the orthodoxy they perform. The difference between there and then and China now is that there is no shared consensus that the West has the better answer, but rather a shared hope to find the resources at home.

The variety of non-elite pronouncements reflects two primary realities of ideological life in the CCP: the pervasive power of nationalism and a broadly recognised crisis in morality.

Choices, Dilemmas, and Risks for Chinese Leadership after the 18th Congress

The installation of a new Chinese leadership headed by Xi Jinping in November 2012 marks a potential turning point in China's political and economic developments. The operative word in this statement is "potential". While the need for significant, if not fundamental, policy adjustments or reforms is overwhelming, the probability that the new leadership will actually pursue such changes remains unclear, in spite of its pro-reform rhetoric in the last few months. At this stage, the analytical community can do no more than take stock of the new political alignment at the top of the Chinese government, identify its most urgent policy priorities, analyze the political obstacles to possible reforms, delineate probable options, and assess their risks.

This briefing paper is divided into four sections. The first section briefly examines the new leadership line-up. The second section reviews Xi's major policy pronouncements and attempts to decode his long-term intentions. The third section identifies the most critical policy priorities facing Xi and his colleagues and outlines possible policy options and dilemmas awaiting them in the next three to five years. The final section assesses the risks associated with the political options the new leadership is most likely to choose.

The new leadership: a brief review

As expected, the new top leadership of the Chinese Communist Party (CCP) is carefully constructed to balance the interests and power of competing factions (although we must admit that the factional lines are not clearly drawn or visible from the outside). In all likelihood, the basis of factions at the top is not institutional or ideological, but personal. Given the enormous influence of powerful individuals in the process of picking members of the Politburo and its standing committee, it is safe to speculate that personal ties, not institutional interests (defined here in terms of representing the interests of the military, certain industrial sectors or political groups), determine who gets selected to fill those positions. Institutional connections may matter, but only to the extent that individuals happen to form their bonds and trust while they work in the same organizational setting, such as the Communist Youth League, a training platform for a large number of China's elites.

Based on this perspective, it seems reasonable to conclude that the new seven-member Politburo Standing Committee reflects the personal influence of the former leader Jiang Zemin, who managed to place three of his loyalists (Zhang Dejiang, Yu Zhengsheng, and Liu Yunshan) on the committee. Zhang Gaoli may also be counted as a Jiang protégé. However, it is important to point out that there is overlapping of personal ties at the top. Liu and Zhang may be closer to Jiang, but they are also acceptable to Hu. Another, albeit often neglected, point to remember is that personal ties can shift.

Retired leaders such as Jiang may not be able to count on the loyalty of their protégés. An assertive top leader—and the just-retired leader Hu Jintao is not one—can change the political dynamics in the Politburo Standing Committee. What this analysis implies is that we should not take the current line-up in this committee as evidence that Jiang will be the power broker for the coming years. In fact, Jiang's influence has probably peaked. His old age and Xi's apparent self-confidence and assertiveness will force Jiang's protégés to decide to seek new allies at the top. The conventional wisdom regarding the Politburo is that while Hu apparently has lost his battles to put people on the standing committee (eg, Li Yuanchao), he received his consolation prize by appointing many of his loyalists to the Politburo; depending on how one counts, Hu's loyalists now comprise probably a third of the latter. In particular, Hu succeeded in promoting Hu Chunhua, 49, to the Politburo, giving him a head start in competing for one of the two top leadership slots in the post-Xi era. The most important thing to know about the new Politburo is that its most senior members are well positioned to fill the five seats on the standing committee that will be vacated by retirements in 2017. Both Li Yuanchao and Wang Yang will be front-runners. The CCP will also pick two people to succeed Xi and Li Keqiang. The focus of the competition for succession in 2017 will definitely be the appointment of the two "leaders-in-waiting". At the moment, Hu Chunhua and Sun Zhengcai, the new Chongqing party boss and Politburo member, are seen as front-runners. But it is premature to conclude that the top slots are theirs to lose: the final decision will not be made until the middle of 2017.

The make-up of the Politburo and its standing committee suggests a high degree of political fluidity. Many possibilities exist. The most decisive factor is whether Xi can exert his personal influence and re-set the CCP's political agenda.

Xi's recent performance and possible intentions

If we look at Xi's performance as China's top leader since his formal appointment in mid-November last year, he seems to have got off to a strong start on three salient issues: anti-corruption, economic reform and populism. In addition, he has also succeeded in building very quickly the image of a confident and decisive leader. While Xi has received high scores for these measures in the Chinese domestic media, and perhaps amongst many ordinary Chinese, it is important to note that his actions so far consist of mostly rhetoric and symbolic gestures. Specific policy measures have yet to be formulated (to be fair, he has not had enough time).

The question on our minds is what kind of leader Xi wants to be. There are three possible models for him, all from the former Soviet Union: Leonid Brezhnev, Yuri Andropov and Mikhail Gorbachev. The Brezhnev model, characterised by stagnation and hostility to the West, does not seem to be a path Xi wants to follow. To the extent that critical reforms failed to take place, Hu's decade is now commonly compared to a decade of lost opportunities and even stagnation. Although Xi himself has not directly attacked his predecessors, his recent speeches did not conceal implicit criticisms of their conservative policies. Given Xi's strong rhetoric on mustering the political courage for reform, the Brezhnev model is unlikely to be in China's future.

Rejecting the Brezhnev model may be easy but replacing it with a more promising strategy is much harder. For Xi, the real challenge is how to guide China forward while ensuring stability. He could try the Gorbachev model by mobilising the masses politically to overcome opposition to reform from entrenched interests. This, as we well known, is a high-risk strategy. Amongst China's top elites, the Gorbachev model is a much-reviled concept because it was blamed for the collapse of the Soviet regime. Xi, given his background as one of the inheritors of the legacies of the Chinese communist revolution, is unlikely to be considering a strategy that could sweep the CCP into the dustbin of history. Xi's reluctance in embracing political reform can be seen in his rhetoric. Remarkably, for all his talk about the need to reform, he has so far studiously avoided mentioning political reform as an option or objective. If, as reported in *The New York Times*, Xi privately vowed to avoid a Soviet-type collapse with stricter adherence to the party's core principles (ie, maintaining its political monopoly at all cost), he should not be counted upon to make fundamental political changes.

> *Judging by Xi's rhetoric, it appears that his political agenda may closely resemble that of Andropov: economic reform without political change.*

That leaves Xi only with Andropov as a possible model. What makes that model potentially appealing to Xi is that Andropov did not try to introduce democratic reform, as Gorbachev later did. His strategy was to strengthen the late-communist system with stricter enforcement of discipline and technocratic reform, not replace it with democracy. Judging by Xi's rhetoric, it appears that his political agenda may closely resemble that of Andropov: economic reform without political change. Obviously, this strategy is by no means new in China. The late Deng Xiaoping was a firm believer in this approach.

Policy choices and dilemmas for the new leadership

The most obvious challenge to a possible Andropov model is that its success is far from assured. While the need for major structural economic reforms is recognised within the regime, the obstacles to such reforms are considerable. In the short-term, Xi's greatest enemy is not the liberals demanding democracy, accountability and social justice, but the conservative elites inside the CCP who have benefited enormously from China's unique form of state-dominated crony capitalism. Economic reform today is unlikely to succeed without reducing the power and privileges of the political elites. Accomplishing this difficult feat is impossible without mobilising forces outside the regime—in other words, democratically empowering the Chinese people. This will be the most difficult dilemma for the Xi leadership: how to implement the economic and social reforms critical to the long-term survival of the regime without unleashing dangerous political forces within Chinese society.

He may first try to accomplish the impossible by relying on moral suasion and selective use of anti-corruption prosecution to send a message to the members of the elites who are not complying with his wishes. In the current political context, where the ruling elites are incorrigibly cynical and venal, moral or ideological exhortations are unlikely to change behaviours. Targeting uncooperative officials with anti-corruption prosecution has limited effectiveness because of the high degree of politicisation of the anti-corruption system. Well-protected members of the elites may have little to fear from the threat of an anti-graft campaign. In all likelihood, based on their correct observation of similar past campaigns following the installation of a new leader (the number of anti-corruption prosecutions typically double in the first year of the new leader's term but revert to normal in his second), they may feign compliance initially but quickly go back to business as usual.

This analysis would suggest that the most critical decision point for Xi will come in his third to fourth year in office—when he finds that his early initiatives are going nowhere or delivering poor results because of opposition from the elites. The question is whether he will have that long to establish his credibility and maintain confidence in his leadership, and whether Chinese society will be patient enough for major changes.

Likely scenarios: events driving policy, not the other way around

The pressures for change building up in Chinese society are not likely to allow Xi to enjoy a long "honeymoon". He will have to deliver real results quickly. At the moment, he faces dangers on several fronts.

First, his pro-reform rhetoric raises expectations but his political capital and skills are insufficient to make real changes and meet these expectations. Disappointment could set in as quickly as in his third year in office. In other words, the make-or-break moment for Xi is 2014 when the policy pronouncements expected to be made in the fall of 2013 (when the third plenum presents a new policy agenda that fully reflects his goals) are put into action.

Second, China's liberal forces will probably not give Xi a free pass. They will find opportunities to test Xi's commitment and ideological leanings. Incidents similar to the anti-censorship protest in Guangdong in January will likely be repeated in the coming year or two, forcing Xi to show where he stands. In the *Southern Weekly* incident, during which the state was seen to interfere openly in the newspaper's editorial line, Xi managed to hold a middle course, to no one's satisfaction. Should Xi face challenges from the liberal side, he will be forced to decide whether to use repressive means and stifle the demands for political reform or to respond and start liberalising controls over the media and civil society. The political risks for Xi would be significant because his conservative colleagues could undermine his authority if the small steps taken by Xi to open up the political system quickly mushroom into large-scale expressions of opposition to the party's rule.

Third, the Chinese economy may experience a financial crisis due to the build-up of bad loans in the banking system over the last five years. The persistent deceleration of economic growth will likely set off a chain of events leading to defaults, bankruptcies and unemployment. If a significant adverse economic event occurs, it will likely scramble any pre-conceived plans Xi and his colleagues may have for the coming five years. Of course, such an event may also provide a strategic opportunity to implement difficult economic reforms. However, the bottom-line assessment is that in the coming two to three years in China, events, not policy, will drive the politics and leadership behaviour in China.

Rising Tensions? Youth and Popular Culture, Consumerism and the Future of China's Social Contract

At the beginning of 2013, several months after the tumultuous events in Chinese elite politics leading up to the installation of a new leadership team at the 18th Party Congress, major Western journals offered "debate" symposia on China's political future, asking pointedly if Chinese communism could "survive" and if a "tipping point" had been reached. Leading newspapers noted the social contract that had been in place in the aftermath of Tiananmen in 1989, under which an apparent consensus had formed that favoured putting economic policy and the almost single-minded pursuit of affluence ahead of ideology and politics. They then suggested that even the "veneer of consensus is breaking down," with an uncertain future that could include "greater political openness, an authoritarian clampdown to restore the veneer of stability, or social turmoil[2]". This recent discussion is closely related to the familiar scholarly debate about the Chinese Party-state and state-society relations. This debate pits those who see the Party-state as "fragile" and under tremendous pressure from public opinion and social forces, particularly in terms of foreign policy decision-making against those who see a "smart" state adapting skilfully to a "strong" society. Indeed, the dominant framework for understanding Chinese politics and state-society relations since around 2003—"authoritarian resilience"—is being increasingly questioned, at least in the West. Within China as well, changes appear to be afoot. These are early signs of a more interesting and even assertive media taking advantage of the leadership change; they are also mixed signals from Xi Jinping that at least some political reform may be necessary and that the pursuit of corrupt officials will include "tigers" as well as "flies", while also warning in private sessions of the necessity for the Party to return to traditional Leninist discipline and combat ideological heresy[3].

Arguably, the most crucial audience for these potential changes is China's young generation, defined here as those born in the 1980s (the "post-80s"), numbering around 240 million (ca. 18.5% of the population) and the 1990s (the "post-90s"), numbering around 140 million (ca. 10.7% of the population). As Chairman Mao well understood, winning the hearts and minds of China's youth is crucial to the sustainability of the Party-state, particularly in an era where state legitimation is no longer based on ideology, but on performance, and where the proliferation and popularisation of social media has placed state policies under far greater scrutiny and criticism. What do youth believe? What do they want? How effective are the CCP's efforts to socialise them so that they will adhere to state-sanctioned values? Examining state policies, media reports, popular culture, interview and survey data, as well as restricted circulation (*neibu*) and other specialised journals provides a complex answer to these questions, not least because state policies and messages are often contradictory, as are the values that can be seen in the attitudes and behaviour of the youth.

> *...many youth...are reluctant to take higher paying jobs they consider beneath their status.*

While it is difficult to generalise about an entire generation, data from surveys reveal a variety of contradictions that mark Chinese youth attitudes and behaviour. For example, many youth, particularly university graduates, are most concerned about economic remuneration when looking for jobs. At the same time they are reluctant to take higher paying jobs they consider beneath their status; they remain unimpressed by most belief systems and privilege their own needs and wants over the needs of society. On the other hand, they can be suddenly motivated to act selflessly when China faces a threat, either external or, in the case of the Sichuan earthquake, from a natural disaster. They display their political support, despite their lack of ideological beliefs, by seeking to join the Communist Party, but do so for very pragmatic reasons relating to future success. They are also consciously aware, but unconcerned at how influenced they have been by Western cultural concepts and the political messages such cultural concepts convey.

These contradictions can also be seen in how Chinese youth see the West, particularly the United States, and how this relates both to the tension between consumerism and nationalism, and regime responses to the contradictions. Chen Shengluo, a Chinese academic who does surveys on university student attitudes toward the US and other countries, noted the existence of “two Americas” in the minds of Chinese students, an “hegemonist” America on the international stage and an America in which a high level of development has been achieved at home because of its values and social system. American culture could succeed in China only because the students could accept this separation. Indeed, when the NATO-led US forces bombed the Chinese embassy in Belgrade in May 1999 during the war in Kosovo, the Chinese media tried to link the hegemonist US with the cultural US. It asserted that everything from American blockbuster films to the promotion of human rights and globalisation, not to mention “Western civilisation” more generally, was part of a deliberate conspiracy by America to control the world. Surveys done in China soon after the bombing strongly suggested, however, that such governmental efforts were unsuccessful, that popular disillusionment toward US and Western culture was short-lived.

The CCP's dilemma has been highlighted in more recent survey work done by Chen, which explicitly compared China and the US in the sensitive area of politics, finding, to his great surprise, that elite university students in Beijing had a decided preference for the American political system over the Chinese system. In particular, they admired the separation of powers. In his sample of 505 students at Beijing's best universities, 31.7% liked the separation of powers a great deal and 43% liked it somewhat. When those who chose "so-so" (*yiban*) are added, the total comes to 95.8%, with only 4.2% choosing "somewhat dislike it" and not a single student choosing "entirely dislike it". Chen interpreted these results as an indication that the students felt the Party's monopoly of power would never be able to solve the problem of official corruption—the number one grievance in Chinese society according to many surveys—and that the American system did a better job in this regard. His findings are congruent with the internal government survey noted above that found well over 80% of university students at 33 universities agreeing that Western visual culture products propagate Western political concepts and lifestyles, and only 17% noting they "don't identify with them".

There are many examples of the inroads of Western popular culture into China, and Chinese government attempts to ameliorate its success and effects. Perhaps most prominent are Hollywood films, which officially constituted 49% of China's film market in 2012, down from 63% in the first half of the year. In addition to such market-controlling devices as screen quotas and blackout dates during the busiest times of the year—which tend to be reserved for Chinese films, including "patriotic" films—other mechanisms include opening two Hollywood blockbusters on the same day to minimise the success of each, removing unacceptable content prior to theatrical distribution and "stealing" the box office through "ticket switching". Western TV shows and Western performers have been popular, even influencing daily speech, as in the case of Lady Gaga, and Chinese television programming. Even political actions, such as the "Occupy Movement", have made their way to China.

In an internal speech in October 2011 at a Central Committee plenum, later given wide publicity upon publication in a major Party journal in January 2012, Hu Jintao railed against the penetration of Western culture into China, and noted that the West and China were engaged in an "escalating war". China, he noted, must respond to the "strategic plot" to Westernise and divide the country, with the ideological and cultural fields seen as the "focal areas of [the West's] long-term infiltration". In contrast to the strong culture of the West, the international influence of Chinese culture "is not commensurate with China's international status". Indeed, to take just one indicator, according to the first *Blue Book on Chinese Soft Power Research*, published in February 2011, the Chinese cultural industry takes up only 3% of the world market, with American culture making up 43%, the European Union 34% and Japan at 10%. In response, China has devoted close to $10 billion a year to enhance its soft power.

However, the contradictions go well beyond popular culture. Political legitimacy depends in part, arguably a large part, on raising the standard of living for Chinese citizens and increasing their wealth and quality of life. Aspirations to join the middle class are high, with many popular books and surveys documenting this desire. Conspicuous consumption and surveys of the super-rich are featured in popular magazines and on such popular television shows as "*If You Are the One*". At the same time, the CCP is concerned about the growing gap between rich and poor and the backlash against inequality, and there have been surveys and best-selling books that show public discontent on this issue. In addition, popular magazines have done surveys and cover stories on the lack of interpersonal social trust. The ineffectual response at the annual National People's Congress meetings has been the slogan, "Don't Worry, Be Happy". Thus, one sees bans and fines against luxury advertising alongside Ferrari and Maserati dealerships in Beijing, but this is hardly a deterrent.

It is certainly clear that the leadership is aware of the negative social effect of these contradictions and the impact on long-term legitimacy and stability, which requires the maintenance of strong economic growth and providing upward mobility for a sceptical, secular younger generation. Articles in restricted-circulation journals intended for policy-makers and Party officials note the challenges the CCP faces in appealing to China's youth. One report by a researcher at the Chinese Academy of Social Sciences (CASS), in contrasting post-80 youth to those born in the 1960s and 1970s, noted that the former lacked a sense of history and a sense of responsibility, that no matter whether post-80 youth seemed to support Communist Party leadership, displayed enthusiasm for multi-party Western political systems or exhibited patriotic activities, in the end they would support whatever political system served their own interests and would exhibit behaviour that led to practical benefits for them. Moreover, their resentment over job prospects, low wages, rising property prices and economic inequalities, particularly among less skilled youth, is viewed as posing an increasing threat to social order[4]. Another internal report noted that most university students were concerned primarily with their own lives and professional goals, with only about 10% concerned with social ideals or morality[5]. The leadership also realises that the post-80s and post-90s generations have access to competing domestic voices with large followings, such as blogger Han Han, and an international cultural marketplace, and that it has become necessary to allow, within limits, such cultural forces, which may present unwelcome messages, to co-exist and compete with state-sanctioned values, in order to maintain any credibility among Chinese youth.

Although it is far too early to talk of a liberalising trend, there have been some preliminary indications that the new leadership may be willing to make some adjustments, particularly within the media. For example, Chinese Central Television (CCTV) has made some interesting changes in the evening news program, the National News Bulletin, and the "Focal Point" program to downplay overt political messages and make the shows more viewer-friendly. Perhaps the greatest stir was caused when CCTV heavily promoted the showing of the Hollywood film "*V for Vendetta*", which had been banned for many years; netizens reacted with disbelief, although whether this was a one-off or a sign of loosening censorship remains to be seen. Other recent developments that have attracted attention are the response to the *Southern Weekend* (*Nanfang Zhoumo*) censorship issue and the cover story on human rights lawyer Pu Zhiqiang in a widely circulated popular magazine, albeit one affiliated with the same group as *Southern Weekend*.

Looking at the key issue of social unrest and instability, now that mass incidents and street protests have become relatively common, arguably the biggest challenge to the regime is to prevent "sanctioned" protests—such as the protest against Japan over the Senkaku/Diaoyu Islands—from being used to promote unacceptable agendas affecting domestic political issues. Efforts must be made to ensure that protesters do not link up over broader geographical and issue areas, and maintain elite unity so that, for example, a future Bo Xilai is not tempted to play the populist card and appeal directly to a "restless" public for support.

Dreams and Ghosts: Assessing the "Social Mood" in Today's China

Since Xi Jinping's appointment as General Secretary of the Chinese Communist Party (CCP) at the 18th Party Congress in November 2012, much attention has focussed on the strength of his reforming zeal, in particular his commitment to combating corruption. There has also been much speculation about whether he will harden China's foreign policy and security stances, but Xi knows very well that many of his challenges are internal. Some of them are philosophical.

When Xi Jinping appeared in front of the press to present the new Standing Committee of the Politburo at the end of the Party Congress to announce his own appointment, he spoke simply and directly about the aspirations of ordinary Chinese people, "our people love life and expect better education, more stable jobs, better income, more reliable social security, medical care of a higher standard, more comfortable living conditions and a more beautiful environment. They hope their children can grow up better, work better and live better. People's yearning for a good and beautiful life is the goal for us to strive for." He has also coined the catchphrase the "Chinese dream", leading to a great deal of expert speculation and online discussion about Xi's understanding of it—and indeed about the views of ordinary Chinese people about the Chinese dream.

So is this the beginning or the end of the Chinese dream? What are the dreams of ordinary Chinese people? In 2007, a researcher visited Chongqing to find out and uncovered a well of insecurity and fear, even despondency about the future. In the 1980s there had been general optimism in the cities and the countryside. People began to aspire to a Chinese dream of a house, a car, travel, economic security and personal and social freedom for themselves and their families. Above all, after the turbulence of the late 1960s and the rapid implementation of reforms, people hoped for freedom from tragic social convulsions of the sort they had experienced in the Great Leap Forward and the Cultural Revolution, the latter still vivid in many people's memories. Ordinary people hope for peace of mind. To achieve that the government has to reform longstanding policy stances like the one-child policy, household registration for urban migrants and legal and procedural fairness for citizens with complaints and grievances.

While travelling around China in 2007 the researcher saw many ordinary people place their wishes on trees in temples, hoping that the wind will blow their prayers to heaven. This presented an opportunity to assess the country's "social mood" informally. Four questions were printed on postcards shaped like leaves: Who are you? What event changed your life? What is your greatest worry? What do you wish for? Hundreds of people answered the questions and pinned their leaves, with their answers, to the trees. Not scientific research, but nevertheless the views of ordinary people in their own words without restraint or control.

For some people, new prospects had clearly opened up. For them, change had been a good thing, although they still had their anxieties:

> *"I work for a private enterprise. Walking out of the state-owned enterprise [changed my life. My greatest worry is] no money. [I wish] to have loads of money."* (Woman, 24)

That woman had abandoned the old economic structures and entered the emerging Chinese economic norm. Similarly with this man

> *"I'm a sales manager. I joined Coca-Cola Chongqing branch in 2002. I worked hard and got promoted. Being honest and hard-working changed my life. [My worries are] getting ill; social security. [I wish] to help people with difficulties."* (Man, 28)

These are people signing up to a "Chinese dream", but these positive responses were far outweighed by descriptions of loss of security and fears for the future.

Most of the 1400 responses told me about a range of anxieties: worries about costs of health care, for example, and, if they had lost their job, anxiety about having no health insurance. Even those with health insurance were concerned that cash limits would not cover the costs of a serious or persistent illness requiring expensive treatment. People who had lost their jobs feared that they would never have the skills to get another one. This man, who was 52, had lost out twice, losing out on his agricultural past and then losing his factory job.

> *"I was a worker at the tire factory and I changed from rural to non-rural urban registration and the tire factory went bankrupt. I'm already in my fifties and I'm getting old. It's very hard for me to find a job. I don't have enough money for food and my living expenses. I don't see a way to solve my problems and we don't have health insurance…I can't*

> *even afford my living expenses and I need to support my parents. I don't know what to do [I wish] to get some compensation and to get health insurance when I retire."*

Old people, particularly those who had lost their jobs before retirement, feared that their pensions were too low and, again, if they got sick, they could not afford the treatment. For all three generations, these anxieties were gravely exacerbated by the one child policy. Children bear all their parents' and grandparents' expectations alone. As this 59-year-old woman said,

> *"I'm worried about the medical problems because we are a one-child family. I hope I can be taken care of when in illness and the retirement salary will increase at the same rate as food prices rise."*

The middle generation care for their child and parents without the support of siblings, and elderly people face the insecurities of old age with only one child to turn to. This man was 43 years old and in the middle of cares and anxieties about the generation above and below him.

> *"[My greatest worries are] medical care and social welfare for the elderly. I hope my daughter will be selected by the university after her examinations. I hope my family will be secure and happy."*

Parents worried about the costs of education. As this 36-year-old mother said,

> *"[My greatest worry is] the tuition fee for my son to go to university will be too expensive."*

Children agonised about meeting their parents' expectations. This boy was worrying about his academic prospects at the age of 11.

> *"I'm worried in the future I will not be a good student and I will disappoint my parents. I hope I can go to university and make a positive contribution to my homeland."*

How do people cope? One option is to save as much as possible. The savings rate in China is amongst the highest globally. The age-savings pattern is also different. In most countries people save the largest amount in middle age, when incomes are highest and expenditure on raising children begins to decline. In China, by contrast, people generally save most as young adults, to pay for their child's education, and when they are old, as a hedge against the costs of getting ill. People also complain and protest, for example, about land confiscations, unpaid wages and environmental damage.

Unable to cope, some find refuge in the forms of decadence and amnesia familiar in the West, some of which also have deep roots in Chinese cultural history: drugs, gambling and prostitution—all increasing. Barber shops in Beijing double as brothels after hours. Others turn to religion. Not banned like in the Mao years, although still requiring official permission, all religions are on the rise: traditional Buddhist and Daoist observance, as well as Christianity, including Catholicism and new sects and cults. In the Taiping and the Boxer rebellions, China has a rich history of religious resistance. Falun Gong protesters set themselves on fire protesting against suppression of their beliefs. Tibetan Buddhists have recently adopted the same self-immolation tactic to draw attention to their feeling that their religion, culture and identity are under threat. Nationalism, as in the protests about the islands disputed with Japan is also a genie that emerges angrily and uncontrollably. Failing all else, people commit suicide. In most countries, young men who live in cities and suffer from mental illnesses are most likely to commit suicide. In China, this afflicts predominantly women living in the countryside, seemingly chafing at the restraints and restrictions of poverty and hidebound tradition.

Many people resort to what James C. Scott, a professor of political science and anthropology at Yale University, calls the "weapons of the weak". They complain, without much hope that their complaint will be heeded or redressed. They ridicule their superiors. They gossip and intrigue. They become cynical and dismissive. All are expressions of discontent, even if not overt political protest.

Reducing social unrest does not only depend on human rights and democracy, as Western liberals too readily believe. Some grievances are about policy, not politics. If the government wanted citizens to feel that the powerful were on the side of the people they could ensure that there was procedural fairness and rule of law for legitimate complaints. The authorities could also relax the one-child policy in places where the fertility rate has now fallen below the replacement rate. They could relax household registration requirements (*hu kou)* so that rural families could be reunited with the migrants who have moved to the cities looking for work. However, social policies are more difficult to implement than building infrastructure. They are people-centred, rather than building-centred, and so harder to predict. Social policy priorities are also contradictory and difficult to reconcile. How can the government reconcile creating jobs with environmental sustainability for example? Regional variations also mean that social policy cannot be centrally run from Beijing and that requires clean, efficient local government. As the Chinese government faces the uncertainties of a leadership transition, the unity of purpose, policy consensus and sense of urgency about decision-making become harder to achieve. Politics makes policy more difficult.

But the Party faces an even more profound philosophical difficulty. Each leader adopts a set of optimistic slogans and seeks over time to populate those catchphrases with ideas which will eventually enter Party orthodoxy. Deng talked about "reform and opening". Jiang Zemin promoted the "three represents", which opened the door to business people and entrepreneurs becoming senior Party officials. Hu Jintao, echoing Sir Francis Bacon, the 17th-century English exponent of scientific methods and an admirer of Chinese technological achievements, promoted the "scientific path to development" and the neo-Confucian idea of the "harmonious society". And now Xi Jinping talks of the Chinese dream. No Chinese Communist leader, including Mao or Zhou Enlai, promoted an understanding or narrative of loss. Blanket optimism about progress is obligatory. Change is never a setback, much less disastrous; not even ambiguous. The gap between that rhetoric and the reality of people's lives has created "cognitive dissonance" which borders on cynicism; a sense that leaders are at best out of touch or at worst complicit personal beneficiaries of a system that disadvantages the many in the interests of the few. It is the Party's moral legitimacy as much as its economic competence which will be most severely tested in the near future.

The editing out of loss does not just apply to future scenarios promoted by leaders. Collective memory is also edited. The Cultural Revolution has been roundly denounced, because neither Deng nor any of his successors were implicated but the Great Leap Forward has been sanitised in the official discourse to exonerate Deng and Zhou Enlai. Tiananmen is taboo. But memories cannot be erased. Repressed memory becomes trauma and in defiance of attempts to forget the troubling past resurfaces in Chinese mythology as hungry ghosts.

Why China Cannot Rise Peacefully

China's rise over the past thirty years has been meteoric and there are many who believe it will continue its impressive growth in the decades ahead. Of course, there are doubters, who think China has significant problems at home that will seriously hamper its economic growth. If the pessimists are wrong, however, the rise of China will almost certainly be the most important geopolitical development of the 21st century. The attendant question that will concern every foreign policy-maker and student of international politics is a simple but profound one: can China rise peacefully?

My answer is no. If China continues its ascent over the next few decades, China and the United States are likely to engage in an intense security competition with considerable potential for war. Most of China's neighbours, to include India, Japan, Singapore, South Korea, Russia and Vietnam, will join with the United States to contain China's power.

What is the basis for this conclusion? To predict the future in Asia, one needs a theory of international politics that explains how rising great powers are likely to act and how the other states in the system will react to them. The main reason for relying on theory is that we have no facts about the future, because it has not happened yet. Thomas Hobbes put the point well: "The present only has a being in nature; things past have a being in the memory only, but things to come have no being at all". Thus, we have to rely heavily on theories to predict what is likely to transpire in world politics.

My theory of international politics says that the mightiest states attempt to establish hegemony in their region of the world, while making sure no rival great power dominates another region. After laying out the theory, I will try to show its explanatory power by applying it to US foreign policy since the country's founding. I will then discuss the implications of the theory and America's past behaviour for future relations between China and the United States.

The basic theory

Survival is a state's most important goal. It can pursue other goals like prosperity and protecting human rights, but those aims must always take a back seat to survival, because once a state is conquered it is unlikely to be in a position to pursue any other goals. Stalin put the point well during a war-scare crisis in 1927: "We can and must build socialism in the USSR. But in order to do so we first of all have to exist". Because states want to maintain their sovereignty, they will be motivated to search for ways to enhance their security. The basic structure of the international system forces states concerned about their survival to compete with each other for power. The ultimate goal of every great power is to maximise its share of world power and eventually dominate the system.

The international system has three defining characteristics. First, great powers are the main actors in world politics and they operate in an anarchic system. This is not to say the system is characterised by chaos or disorder. Anarchy simply means there is no centralised authority or ultimate arbiter that stands above states. The opposite of anarchy is hierarchy, which is the ordering principle of domestic politics.

Second, all great powers have some offensive military capability, which means they have the wherewithal to hurt and possibly destroy each other. In other words, states are potentially dangerous to each other, although that capability varies among states and for any state it can change over time.

Third, states can never be certain about other states' intentions. They ultimately want to know whether other states are determined to use force to alter the balance of power—revisionist states—or whether they are satisfied enough with it and have no interest in using force to change it—status quo powers. The problem, however, is that it is almost impossible to discern another state's intentions with a high degree of certainty. Unlike military capabilities, intentions cannot be empirically verified. Intentions are in the minds of decision-makers and they are difficult to know for sure. But even if one could determine another state's intentions today, there is no way to determine its future intentions. It is impossible to know who will be running foreign policy in any state five or ten years from now, much less whether they will have aggressive intentions.

In a world where other states might have malign intentions as well as significant offensive military capabilities, states tend to fear each other. That fear is compounded by the fact that in an anarchic system there is no night watchman for states to call if trouble comes knocking at their door. Consequently, states recognise that the best way to ensure their survival is to be especially powerful. The reasoning here is straightforward: the more powerful a state is relative to its competitors, the less likely it is that it will be attacked. No country in the western hemisphere, for example, would dare strike the United States because it is so powerful relative to its neighbours. This simple logic drives great powers to look for opportunities to shift the balance of power in their favour. But great powers do not merely strive to be the strongest great power, although that is a welcome outcome. The ultimate aim is to be the hegemon, that is, the only great power in the system.

What exactly does it mean to be a hegemon in the modern world? It is almost impossible for any state to achieve global hegemony, because it is too hard to project and sustain power around the globe and onto the territory of distant great powers. The best outcome a state can hope for is to be a regional hegemon, and thus dominate one's own geographical area. The United States has been a regional hegemon in the western hemisphere since the late 1800s. Although the United States is clearly the most powerful state on the planet, it is not a global hegemon.

powers in other geographical regions from duplicating its feat. A country that dominates its region does not want a peer competitor, mainly because regional hegemons are so dominant in their own backyard that they are free to roam around the world—think about the United States today—and cause trouble in distant regions. A state that achieves regional hegemony wants to make sure no great power in another region achieves hegemony and is thus free to roam into its backyard. The United States, for example, intensely dislikes the idea of distant great powers operating their military forces in the western hemisphere. Thus, regional hegemons prefer there be at least two great powers located together in other regions, because their proximity will force them to concentrate their attention on each other rather than the distant hegemon. In sum, the ideal situation for any great power is to be the only regional hegemon in the world.

The American story

A brief look at the history of American foreign policy illustrates the power of my realist theory. When the United States won its independence from Britain in 1783, it was a small and weak country comprised of thirteen states strung out along the Atlantic seaboard. The British and Spanish empires surrounded the new country and hostile native American tribes controlled much of the territory between the Appalachian Mountains and the Mississippi River. It was a dangerous threat environment for sure.

Over the course of the next 115 years, American policy-makers of all stripes worked assiduously to turn the United States into a regional hegemon. They expanded America's boundaries from the Atlantic to the Pacific as part of a policy commonly referred to as "Manifest Destiny". The United States fought wars against Mexico and various native American tribes and took huge chunks of land from them. At different times, US policy-makers wanted to conquer Canada as well as territories in the Caribbean. The United States was an expansionist power of the first order. Henry Cabot Lodge put the point well when he noted the United States had a "record of conquest, colonisation, and territorial expansion unequalled by any people in the 19th century". Or, I might add, the 20th century.

American policy-makers in the 19th century were not just concerned with turning the United States into a powerful territorial state. They were also determined to push the European great powers out of the western hemisphere and make it clear they were not welcome back. President James Monroe laid out this policy, known as the Monroe Doctrine, for the first time in 1823 in his annual message to Congress. By 1898, the last European empire in the Americas had collapsed and the United States had become the first regional hegemon in modern history.

However, a great power's work is not done once it achieves regional hegemony. It then must make sure no other great power follows suit and dominates its area of the world. During the 20th century, there were four great powers that had the capability to make a run at regional hegemony: imperial Germany (1900-1918), imperial Japan (1931-1945), Nazi Germany (1933-1945) and the Soviet Union during the Cold War (1945-1989). Not surprisingly, each tried to match what the United States achieved in the western hemisphere in the previous century.

How did the United States react? In each case, it played a key role in defeating and dismantling those aspiring hegemons.

The United States entered World War I in April 1917 when imperial Germany looked like it would win the war and rule Europe. American troops played a critical role in tipping the balance against the Kaiserreich, which collapsed in November 1918. In the early 1940s, President Roosevelt went to great lengths to manoeuvre the United States into World War II to thwart Japan's ambitions in Asia and especially Germany's ambitions in Europe. The United States came into the war in December 1941, and it helped destroy both Axis powers. Since 1945, American policy-makers have gone to considerable lengths to keep Germany and Japan militarily weak. Finally, during the Cold War, the United States steadfastly worked to prevent the Soviet Union from dominating Eurasia and then helped relegate it to the scrap heap of history between 1989 and 1991.

Shortly after the Cold War ended, the first Bush Administration's famous "Defence Guidance" of 1992, which was leaked to the press, boldly stated that the United States was now the most powerful state in the world by far and planned to remain in that exalted position. In other words, the United States would not tolerate a peer competitor. That same message was repeated in the famous "National Security Strategy" issued by the second Bush Administration in October 2002. There was much criticism of that document, especially its claims about "pre-emptive war". But hardly a word of protest was raised about the assertion that the United States should check rising powers and maintain its commanding position in the global balance of power.

The bottom line is that the United States, for sound strategic reasons, worked hard for more than a century to gain hegemony in the western hemisphere. After achieving regional dominance, it has gone to great lengths to prevent other great powers from controlling either Asia or Europe.

What are the implications of America's past behaviour for the rise of China? Specifically, how is China likely to behave, as it grows more powerful? And how are the United States and the other states in Asia likely to react to a mighty China?

Uncle Sam v. the dragon

My theory tells me that if China continues its impressive economic growth over the next few decades, the United States and China are likely to engage in an intense security competition with considerable potential for war. Let me briefly describe how I think China is likely to behave, as it grows more powerful, as well as how the United States and the other states in Asia are likely to react to a mighty China.

China will want to make sure it is so powerful that no state in Asia has the wherewithal to threaten it.

China is likely to try to dominate Asia the way the United States dominates the western hemisphere. Specifically, China will seek to maximise the power gap between itself and its neighbours, especially India, Japan and Russia. China will want to make sure it is so powerful that no state in Asia has the wherewithal to threaten it. It is unlikely China will pursue military superiority so it can go on a rampage and conquer other Asian countries, although that is always possible. Instead, it is more likely that it will want to dictate the boundaries of acceptable behaviour to neighbouring countries; much like the United States makes it clear to other states in the

Americas that it is the boss. Gaining regional hegemony, I might add, is probably the only way China will get Taiwan back.

An increasingly powerful China is also likely to attempt to push the United States out of Asia, as the United States pushed the European great powers out of the western hemisphere. We should expect China to come up with its own version of the Monroe Doctrine, as Japan did in the 1930s.

These policy goals make good strategic sense for China. Beijing should want a militarily weak Japan and Russia as its neighbours, just as the United States prefers a militarily weak Canada and Mexico on its borders. What state in its right mind would want other powerful states located in its region? All Chinese surely remember what happened in the last century when Japan was powerful and China was weak.

Furthermore, why would a powerful China accept US military forces operating in its backyard? American policy-makers, after all, go ballistic when other great powers send military forces into the western hemisphere. Those foreign forces are invariably seen as a potential threat to American security. The same logic should apply to China. Why would China feel safe with US forces deployed on its doorstep? Following the logic of the Monroe Doctrine, would not China's security be better served by pushing the American military out of Asia?

Why should we expect China to act any differently than the United States did? Is it more principled than the US is? More ethical? Less nationalistic? Less concerned about its survival? China is none of these things, of course, which is why it is likely to imitate the United States and try to become a regional hegemon.

It is clear from the historical record how American policy-makers will react if China attempts to dominate Asia. The United States does not tolerate peer competitors. As it demonstrated in the 20th century, it is determined to remain the world's only regional hegemon. Therefore, the United States can be expected to go to great lengths to contain China and ultimately weaken it to the point where it is no longer capable of ruling the roost in Asia. In essence, the United States is likely to behave towards China much the way it behaved towards the Soviet Union during the Cold War.

China's neighbours are certain to fear its rise as well, and they too will do whatever they can to prevent it from achieving regional hegemony. Indeed, there is already substantial evidence that countries like India, Japan, and

Russia, as well as smaller powers like Singapore, South Korea and Vietnam are worried about China's ascendancy and are looking for ways to contain it. In the end, they will join an American-led balancing coalition to check China's rise, like Britain, France, Germany, Italy, Japan and even China joined forces with the United States to contain the Soviet Union during the Cold War.

Finally, given Taiwan's strategic importance for controlling the sea-lanes in East Asia, it is hard to imagine the United States, as well as Japan, allowing China to control that large island. In fact, Taiwan is likely to be an important player in the anti-China balancing coalition, which is sure to infuriate China and fuel the security competition between Beijing and Washington.

In conclusion, the story my theory tells about what is likely to happen if China continues its rise is not a pretty one. Indeed, it is downright depressing. It is worth noting, however, that, while social science theories are essential for helping us to make sense of the world, they are nevertheless rather crude instruments. The ability of even the best theories to explain the past and predict the future is limited. Every theory confronts cases that contradict its main predictions. Let us hope the case of a rising China contradicts my theory.

Future Security Challenges in China-US Relations and Their Long-Term Global Consequences

At the broadest strategic level, the most important and potentially dangerous challenge confronting the Sino-US relationship derives from their emerging bilateral security competition in the Western Pacific. This competition is at present largely indirect and tacit in nature but is becoming more direct, explicit, and hence troubling over time. It is driven by several dynamic trends, most notably China's growing economic, military and para-military capabilities and influence on the one hand, and increasing concerns in many capitals over the possible decline of America's regional military capabilities and presence on the other.

What makes this possible shift in relative power and influence so potentially serious over the long term is that Beijing and Washington hold somewhat different views toward two closely related sets of issues that will decisively shape the region's and the globe's future security:

1. The basic distribution of power within the international system—and especially across the Asia-Pacific—that best promotes stability and prosperity and advances each nation's interests; and

2. The core values and norms that govern the activities of the nations, multilateral agreements, processes and forums that make up the global and regional system.

The former centres on two factors:

- The relative roles played by both the United States and China in the global and regional security architecture (and especially the future of US military and political power and influence in the Western Pacific); and

- The dominant political and security relationships between both powers and between themselves and the other major powers in the system, especially in Asia.

The latter centres on American and Chinese beliefs about such critical issues as:

- Free trade and open access to resources;

- The principles governing international agreements (on issues ranging from WMD counter proliferation to human rights);
- The definition of state sovereignty and humanitarian intervention in the domestic affairs of nation-states;
- The legal principles required to adjudicate various inter-state disputes;
- Definitions of relevant social and political rights; and
- Proper relative levels of voting power in key international institutions held by China (and perhaps other developing nations) compared with the United States and Western democracies.

These two sets of issues are of course to some degree casually related, ie, many norms governing the international system reflect the existing or passing distribution of power among nations. Hence, major changes in power distribution could lead to significant efforts to alter many existing norms.

Changing capacities and relationships

For over six decades, US and some foreign political and military leaders have believed that stability and prosperity in the maritime Western Pacific have relied, and continue to rely, fundamentally on American military—and primarily naval—predominance. These have to be backed by US political leadership and closely allied political and military relationships with regional powers such as Japan and South Korea. This bedrock assumption stands in contrast (some would say clashes) with Beijing's notion that regional (and global) stability and prosperity are best served by a multipolar environment of more or less equally strong and unallied major powers held together in largely peaceful relations through intensifying levels of economic cooperation and the integrative power of globalisation.

Until quite recently, these contrasting assumptions did not exert a major influence on Sino-US relations or the basic stability of the Western Pacific. This is largely because China was too weak to challenge US maritime predominance and because such predominance at various intervals served China's security interests, eg, by counterbalancing the former Soviet Union and preventing the re-emergence of Japan as a regional military power. However, two closely related factors have emerged in the 21st century to cast doubt on the viability of such long-standing notions. First, the United

States might not continue to enjoy the economic and military capacity to sustain what will likely be required to maintain its maritime military predominance in the Western Pacific, *and especially along China's maritime periphery*. Second, China might not continue to accept this predominance.

Both the existing military balance and assessments of likely future trends indicate that, even under worst-case assumptions about America's future economic capacity, it seems unlikely that economic factors will prevent the United States from maintaining an extremely potent military force in the Western Pacific well into the century. But will an economically constrained force still be viewed as predominant? If not, is less-than-clear predominance sufficient to influence China and, more broadly, to ensure regional stability and prosperity while protecting US interests in Asia?

It is possible, although by no means certain, that the combination of continued high levels of Chinese defence spending and expanding military deployments relevant to the Western Pacific, alongside a prolonged period of US economic malaise (and growing demands for the application of US resources to non-defence-related areas), might result in both a perceived and actual loss of unambiguous US military superiority in specific, key areas, perhaps even by 2020. In fact, a growing number of US and some allied defence analysts believe that America's ability to prevail in a Sino-US military conflict over Taiwan is already in considerable doubt and will increasingly depend on both future warning time and out-of-area deployment capabilities, barring a major change in existing force trajectories.

More broadly, if China continues to devote substantial resources to its current program of maritime and related military modernisation, within a decade, China might acquire a credible threat to hold surface warships, including US carriers, at risk not only in the vicinity of Taiwan, but also within approximately 1500 nautical miles of its entire coastline. Equally significant, China is also expected to deploy a large arsenal of short- and medium-range ballistic missiles (SRBMs and MRBMs), submarine, air, and ground-launched land attack cruise missiles (LACMs), and computer network attack capabilities that could pose a credible threat to US and allied bases in Asia, as well as many logistics and support infrastructures. China could even

> *China could even acquire the capability to compete in a significant way for air superiority in areas along its periphery, and perhaps further afield.*

acquire the capability to compete in a significant way for air superiority in areas along its periphery, and perhaps further afield. It might buttress these capabilities by making future gains in the areas of information warfare (IW) and computer network operations (CNO), including cyber-attacks.

These and other developments could:

- Aggravate sensitive regional hotspots such as Taiwan, the Korean Peninsula, and territorial and resource disputes in nearby seas;
- Diminish the effectiveness of carrier-based US assets across much of the Western Pacific;
- Reduce regional confidence in US security guarantees and the US deterrence capacity throughout the region; and
- Produce destabilising security competition between China and other major nearby countries, such as Japan and India.

Alternatively, several Asian countries might gradually become more pro-Chinese in their foreign economic and diplomatic policies and/or less supportive of US policies in the region, especially if those are unable to develop military forces to effectively counter growing Chinese capabilities. This could become a major issue for Japan, given existing financial and constitutional constraints on defence spending and military operations, as well as its growing economic dependence on China.

The uncertainties accompanying such assessments highlight the critical importance of subjective judgements (as opposed to simple force-on-force comparisons) in measuring the presence or absence of US military predominance in maritime Asia, and hence the utility of such predominance for Washington's strategy toward Beijing. Such judgements involve perceptions of relative leverage and the ability to press for political advantages in ways that might demonstrate either growing influence (in the case of China) or declining influence (in the case of the United States).

These questions bring us to the second factor influencing American predominance as a critical element of US strategy toward China: Chinese calculations and behaviour. Despite many actual or potential advances in the capabilities of the People's Liberation Army (PLA), Beijing is not yet actively engaged in deliberate efforts to challenge or replace US military power in Asia or elsewhere. However, as China's overseas power and influence grow, it could increasingly oppose efforts by the United States to maintain its predominance in the Western Pacific. This would serve the purpose of reducing its own vulnerability to possible future American efforts to limit its power and achieving key Chinese security objectives, such as the absorption of Taiwan and the creation of a strong security buffer out to the first island chain. This could become particularly likely if serious Sino-American crises emerge over Taiwan or other territorial issues in that region and if there continues to be a significant perception gap, in the minds of not only US and Chinese observers but also other powers, between a stagnating or declining America and a dynamic, fast-growing China.

Contrasting norms and values

In the 21st century, Beijing—partly in response to Washington's policies but also for its own reasons—has on balance deepened and expanded its formal commitments to many international norms, especially in areas such as free trade, nuclear non-proliferation, human rights and the management of non-traditional security threats such as pandemics and climate change. In all of these, China has to varying degrees upheld, accepted or adapted to prevailing norms, while giving few if any clear signs of attempts to radically revise or eliminate most norms. Beijing has supported these international norms for a mixture of motives, including pragmatic considerations associated with its narrow economic and domestic interests, image concerns and the maintenance of its strategic independence. It has also done so for broader reasons reflecting some level of internalisation of international values.

At the same time, even though Beijing generally supports the structures and norms of the international system, it has also sought to qualify or resisted implementing those international practises that it believes excessively infringe on its sovereignty or might pose serious domestic political or social problems. More important, China has also indicated a desire to *alter* some international norms, including those that directly relate to the existing distribution of global and Asian power. This revisionist tendency has usually been expressed via China's affirmation of the concepts of national self-determination, state sovereignty (including state control over economic activities), and non-intervention in the internal affairs of other countries.

Perhaps most notably for American predominance, China's revisionist views have led it to defend its territorial integrity and espouse weaker nations' right to freedom from intimidation by more powerful states. This has led it to attempt to secure international approval for coastal nations' expanded rights to control the air and seas adjacent to their territorial waters and airspace. In particular, Beijing has shown a willingness to both speak and act in support of new or revised norms that directly or indirectly challenge Washington's existing interest in freedom of the oceans and the ability to conduct surveillance and military operations in what America would regard as open waters. In fact, China's position regarding this issue provides the most notable example of its willingness to reinterpret international norms in ways that directly challenge the *status quo* regarding US military power and, indirectly, Washington's political influence in Asia and elsewhere.

The seeming contradiction of China adhering to many international norms while exhibiting a penchant to reinterpret or avoid implementing norms that conflict with its core domestic interests differs more in degree than in kind from the behaviour of other powers. However, it is the only major power that potentially could challenge basic US norms regarding the exercise of American military—and ultimately political—power in the Western Pacific. Yet, China's stance toward the activities of foreign powers in nearby waters and airspace does not *ipso facto* validate the existence of a broad-based, principled and concerted Chinese opposition to the US position in Asia. In other words, it is by no means a foregone conclusion that China will espouse, as a matter of national necessity, alternative *norms* for the international system that directly challenge US maritime predominance across the entire Asia Pacific or that it will undertake actions in support of such a goal.

Nonetheless, the observations made above regarding the sustainability of American predominance and possible changes in China's approach to at least some key norms that directly impact such predominance indicate that the core strategic question for US policy-makers during the coming decades, and perhaps even during the current decade, will be whether and how to maintain clear US military superiority in the Western Pacific and the current pattern of allied political and security relations that support it, or whether to consider (perhaps out of growing necessity) alternative power structures or security architectures as a basis for a new US strategy toward China. Closely related to this question is the issue of whether and how to modify those norms relevant to military activities along the Asian littoral that relate most directly to American predominance.

The future of American predominance

Given the above concerns, some US officials and analysts assert the need for the United States to maintain clear predominance over Beijing at whatever cost, given the uncertainties of the alternatives. Operational concepts such as the highly offensive-oriented, and to some degree pre-emptive "Air-Sea Battle", or the equally ambitious but arguably less dangerous "Offshore Control" are designed to attain that goal. However, such approaches could prove self-defeating, especially given Washington's growing economic limitations, and possibly spur Beijing to increase defence spending above existing high levels, adopt more confrontational foreign and defence policies, and more directly challenge US military capabilities in many areas.

Other US observers recognise these problems and are beginning to assess the future of American predominance in the Western Pacific, but few have offered any specifics. Within the academic world, a growing number of analysts are discussing possible alternative US global and regional security architectures for the long term, including variants of so-called selective engagement, offshore balancing, and cooperative security structures. Unfortunately, each of these alternatives would also present significant problems and uncertainties for the US, China, and other powers. In fact, there is no simple solution to the fundamental security problem outlined above.

Ultimately, any assessment of alternatives to US predominance in the Western Pacific hinges on the answers to three interrelated questions. First and foremost, does the United States have the political will to maintain the economic and technological means to sustain its predominance in the Western Pacific well into the century by recovering in relatively short order from its current economic malaise? If the answer to this question is uncertain at best, then one must ask the following: Can US and Asian political leaders envision and accept an alternative to American predominance in the Western Pacific? Finally, a third question is: What measures, if any, might induce China's political leaders to tolerate or accept US predominance in the Western Pacific, or, failing that, to assist in creating an alternative, stable security system and set of norms in Asia that protect both US and Chinese core interests?

Any answer to these questions cannot rely entirely on assessments of military and economic capabilities. They must also involve assessments—or reassessments—of Chinese and American policies towards a variety of economic, political and security issues. Sustained progress in working together, both bilaterally and multilaterally, to address the growing array of challenges confronting the two countries in many areas, from global economic growth to non-traditional security threats, could greatly increase incentives in both countries to overcome the basic security problems outlined above. For the United States, these activities should involve efforts to develop common standards in many policy arenas that will invest Beijing more deeply into the regional and global system. This will obviously also mean granting China more authority within these systems and coordinating policies between the United States, other key Asian democratic powers and the democracies of Europe.

Such efforts should be directed in particular towards reducing Beijing's incentives to employ its growing military capabilities to manage disputes or to radically and unilaterally alter broader norms and approaches. This will likely require not only the development of varied and deeper forms of political and other types of leverage vis-à-vis China across the region but also a credible means of 1) reassuring Beijing that its most vital security interests will remain unthreatened, while 2) shaping in positive ways China's view of what is required to defend these vital interests, politically, militarily and economically. In particular, more concerted efforts will be required to diminish—not merely manage—those territorial and sovereignty-related concerns that continue to exacerbate Sino-American mistrust.

Update on Sino-European Relations

Relations between China and the European Union (EU) are experiencing a slump that has the potential to cause a breakdown. This short article clarifies the nature of the slump, identifies its causes, and discusses possible futures.

The state of play

Relations between Europe and China have never been so broad, yet it has also been a long time since they were so tense. On the one hand, there has been a continuation of new initiatives in the partnership: two-way investments have continued to grow; European companies transferred back record volumes of investment incomes from China; trade continued to surge and most European member states expect that this trend will be maintained in the coming years; cooperation advanced in the field of research and development; and European companies upheld their position as China's main providers of advanced technology and transferred important know-how through exports, investments and joint-ventures. There has been a proliferation of joint research projects and Chinese actors became prominent participants in programs under Europe's seventh research framework. At the official level, a record number of technical dialogues were already reached in 2006, and the quantity of such exchanges has continued to grow. In 2011 and 2012, new ambitious projects were launched to foster peer-to-peer, SME and youth exchanges. It is no exaggeration to say that the partnership with China has become the most comprehensive and institutionalised of all the European Union's partnerships.

On the other hand, relations have become increasingly tainted by tensions, disappointment and frustration. Both sides have invested a great deal in public diplomacy but mutual perceptions have reached a new low. While the splurge of negative reporting around the Beijing Olympics—focussed on issues ranging from Tibet to poisoned toys and air pollution—subsided, European news media continued to be highly critical of China's evolution. The tone of Chinese news reports about Europe also became more negative, with a lot of emphasis being put on the latter's suspected protectionist preferences and the consequences on China's domestic stability of the EU's inability to tackle the euro-zone crisis. The European policy community, including both member states and European Union officials, largely came to share the position that China had become more assertive as an international actor. Many officials observe a more confident and uncompromising attitude in encounters with their Chinese counterparts.

They also show concern that China's posturing on territorial disputes in Asia is indirectly threatening Europe's security and that growing Chinese nationalism poses a major challenge to global stability. Chinese officials for their part criticise Europe for being unable to act coherently, in spite of the Lisbon Reform Treaty; they also complain that the European institutions have been unable and unwilling to respond constructively to an invitation to set a series of clear priorities for 2020.

Relations have deteriorated most with regards to the economy. Symbolising the souring relations are two major anti-dumping procedures initiated by the European Commission: one against Chinese producers of photovoltaic systems after a complaint from European firms, one against ZTE and Huawei at its own initiative (the so-called *ex officio* procedure). The Chinese side had clearly assumed that it could deflect these procedures by pressuring certain member states to discourage the Trade Commissioner and threatening with repercussions during the high-level economic dialogue. The two cases clearly reflect, on the one hand, that the European Commission has grown impatient with the pace of economic reforms in China, and that it feels increasingly supported by the member states in addressing allegedly unfair competition. Even if it has a mandate to decide on anti-dumping procedures, such a mandate remains politically significant. The two cases were started after several years of criticism by European companies and the Europe-China Chamber of Commerce about the deteriorating business climate in China and excessive trade support. They also followed a steep deterioration of the official exchanges relying on the High-Level Economic Dialogue (HED) and the stand-still of negotiations of several economic chapters in the framework of the Partnership and Cooperation Agreement (PCA). Disappointment, however, has not been confined to the European side. Since 2010, a growing chorus of Chinese diplomats came to lament Europe's unreasonable demands, typically stating that during the HED China only asked "for a few reforms"—pertaining to the visa regime, investments and technology transfer—and that the European side tabled an unrealistically long list of demands. Furthermore, Chinese officials became more and more convinced that the economic troubles in Europe were causing more protectionism.

This more complicated situation has led China to make several new overtures. Whatever their personal disillusionment, Chinese decision-makers understand that a derailment of relations with Europe would be detrimental in light of its tensions with the United States and other Asian regional powers. The top leadership has instructed the Chinese participants in the HED to remain committed. It has also instructed different departments to cooperate with the Ministry of Foreign Affairs to support new exchanges, like the ones addressing clean energy and urbanisation. At the same time, more efforts were invested to keep Germany in the pro-China camp, as well as to curry favour with Central and Eastern European member states using bilateral diplomacy and a regional US$10 billion credit facility. It is clear that China came to regard the latter constituency as particularly relevant in influencing the agenda of the EU, even in comparison with the Mediterranean countries, where many observers assumed it would use debt purchases to gain political leverage. By and large, however, China has not used the debt option decisively to gain influence among the Mediterranean member states. The response on the European side has been inconsistent: it sought to make EU-China ties more productive at the level of high politics, but largely followed the position of the United States on China's role in Asian maritime security. An initiative to define the significance of the EU's strategic partnerships failed.

Explanations

There are four main explanations for the recent slump. First of all, mutual perceptions have never been very positive. When there was talk of a Sino-European honeymoon back in 2004 and 2005, there was mutual excitement but not much confidence and certainly no clear common social, political and cultural aspirations. The excitement hyperbole did continue in the subsequent years, propelled by important events like the 60th anniversary of the People's Republic of China, the Olympics, the Expo and stellar growth figures. But that excitement increasingly has turned negative.

Second, Europe and China never managed to rebalance the economic partnership. The reduction of the trade deficit has been an explicit European demand since the turn of the century but it never materialised. China became more important as an export destination, a source of foreign investment income and a buyer of sovereign debt (an estimated US$500-700 billion in bonds has been bought by China). This could thus not offset the disturbingly large deficits on the current account of the balance of payments. Three factors have contributed to Europe's woes in that sense. There was *the role of large companies* with billions of investments parked in China. These firms generally insisted on maintaining good political relations with China, but in 2010, 2011 and 2012 several of them started to approach their governments informally with complaints of unfair competition. The intention was certainly not to spark a trade conflict and most of them backtracked ultimately, but they did add to the latent misgivings that already exist among officials. There has also been *growing anger among the smaller* *exporting companies* in Germany, France, Italy, Spain, Poland and other important member states. While these firms do not weigh as much as the big ones, they were able to set the tone in important sectors like clean energy and chemicals. Finally, there has been *persistent encouragement from the United States* to take a more forceful position in economic tensions with China.

More fundamentally, the frustration about trade imbalances is a result of the inability to address domestic imbalances, especially on the Chinese side. While the EU could have been criticised for its growing current account deficit and external-debt-driven growth up until the beginning of the euro crisis, it did manage to turn its current account deficits into a mild surplus in the years after. By all standards, the euro zone has managed to curtail its overconsumption. China, meanwhile, did not reduce its excessive reliance on export- and investment-driven growth. Symptomatic of that failure has been its persistently large trade surplus in industrial goods, the increasingly negative position of the corporate sector in the balance sheets of Chinese banks, the record amounts of trade credit disbursed and the fact that the renminbi has hardly appreciated vis-à-vis the euro. While both the European and Chinese economy are under duress, it is clear that China has continued to *externalise* its imbalances much more than Europe.

A third explanation for weakening Sino-European relations is that the political component of the partnership is insufficiently developed to counter some of the economic strains. Europe and China consider each other as strategic partners but the two never identified the geopolitical interests that would underpin such a strategic partnership. If the EU and China both benefit for stability in Africa, the Middle East, Central Asia and the Indian Ocean, this has never been made explicit as a pillar of the relationship. For 2013, the two sides have vowed to intensify the security and defence dialogue, but coordination on Iran, Syria, and the wider belt of uncertainty that surrounds Europe has been modest at best. Regarding the P5+1, Chinese officials find that EU High Representative Catherine Ashton has not been entirely consistent in her approach towards Iran and that she has tended to support Washington's position, leading Beijing to conclude that the issue will still have to be discussed in the first place with Russia and the

> *Europe and China consider each other as strategic partners but the two never identified the geopolitical interests that would underpin such a strategic partnership.*

United States. The P5+1 is viewed as a buffer against possible American unilateralism, not an exemplar of European leadership.

On Syria, Chinese officials are generally satisfied that the West has not yet intervened, but they also express their disdain for Europe's chaotic approach and the plans of France and the United Kingdom to supply arms to rebel groups in the absence of a European Council decision. Beijing does not expect Europe to make a major contribution to the two remote regions where its presence is often criticised: Africa and the Middle East. While the European Union has gained some credit for the anti-piracy operation in the Gulf of Aden, officials criticise it for failing to tackle similar problems in the Gulf of Guinea, promoting stability on the African continent and helping to stabilise Iraq. In all these areas, the United States still figures as the main protagonist. Some Chinese officials and experts have showed themselves impressed by the role of France as a smaller power that continues to wield influence in Africa and successfully maintains a meaningful presence east of Suez. Some also consider France a more reliable and realistic shepherd of Europe's international engagement than the United Kingdom. Yet, again, the expectations of Europe becoming a true international actor remain modest at best.

A fourth and last explanation has been the "feel-good trap". While the first three flaws of the partnership have been present from the outset, China and Europe have tried to overcome them by responding to each setback with a series of new exchanges. This has been particularly promoted by the EU; its summit-driven diplomacy made it eager to establish new avenues for dialogue even when the existing ones were known to be ineffective. Moreover the European Commission and later also the External Action Service have embraced the partnership with China as an important opportunity to demonstrate that they were accepted by the major powers as important institutional actors. Beijing played along and saw in such eagerness an opportunity to avoid a stand-still. Therefore, the proliferation of dialogues kept a large number of officials convinced that there was progress for a while, but several years later it has led to frustration, as progress remains very limited.

The future?

Four important variables will determine whether the nature of the Sino-European partnership can improve. First of all is China's economic rebalancing. If China continues to use its export- and investment-led growth model, supported by assertive "check-book diplomacy", it will inevitably cause more frictions and erode patience amongst pro-China-trade member states and interest groups. The signs are not encouraging. Investments in congested Chinese sectors continue and many senior officials in charge of economic decision-making state that China will have to run a current account surplus for many more years. Second is the political climate in China. If economic imbalances were to lead to social instability, relations with Europe would certainly be damaged. Third are the smaller European powers. The behaviour of smaller states in the Middle East and elsewhere could accelerate the polarisation between China (and Russia) and the West. The main challenge would be a situation in which a Chinese slow-down coincides with more turbulence in strategic regions and adds to the growing distrust between the great powers. The fourth variable is the extent to which the EU manages to reduce the centrifugal forces it faces. The euro crisis has sparked an unprecedented wave of integration, but progress remains frail. Pragmatic elites continue to lose ground as a consequence of the growing polarization between haves and have-nots, which hampers decision-making at the European level even more. The recent slump in relations between Europe and China has thus certainly the potential to turn into a more dramatic break-down.

The People's Liberation Army, the Party and the State: Civil-Military Relations Under the New Leadership

Civil-military relations in China can be analysed along three types of relationships: 1) between the CCP's military elite and civilian elite at the national level (remember: they *all* are Party members); 2) between Party and People Liberation Army (PLA) officials at the sub-national and local levels; and (3) between the PLA and the civilian population. Each of these could consume an entire conference but this summary paper will focus on the PLA as an institutional and bureaucratic actor at the national level.

Does Xi Jinping inherit a PLA that is a "rogue actor?"

The first order of business is to address speculation over the past few years in some quarters of the media and amongst some pundits that the PLA has somehow become a rogue institution, acting independently of, or in defiance of, the Chinese Communist Party (CCP) on defence, military, security or foreign affairs. As we know, there have been various events—some disconcerting and some just bizarre—that have stoked the fires of such speculation. They include 1) the PLA's January 2007 anti-satellite test; 2) a test flight of the PLA Air Force's J-20 fighter during former US Defence Secretary Gates' visit to Beijing in January 2011; 3) the pontifications of some PLA-affiliated commentators in national media in the People's Republic of China (PRC); 4) various incidents in the maritime domain; and 5) the incessant bloviating of the PLA political commissariat reinforcing the time-honoured dictum that "the party controls the gun".

All of the above notwithstanding, there is scant evidence in the public domain that would suggest that the PLA, as an institution, is not loyal to or subordinated under the control of the CCP. Nor is there evidence we can cite that suggests military leaders are riding roughshod over the top civilian CCP leadership, imposing their policy preferences upon a reluctant Party leadership. Finally, it is unlikely that the military is engaged in major strategic-level programs or activities that have not been blessed by the Party.

Speculation about the behaviour of the PLA in Chinese national security affairs oftentimes conflates systemic disconnects, poor policy coordination practises, bureaucratic posturing and lobbying (which are some of the characteristics of the PRC national security policy-making process) with insubordinate behaviour by the PLA.

That said, all is not always black and white, and there is a lot of nuance to this dynamic.

- Does the PLA act as a lobbying group like other PRC bureaucracies? Yes.
- Is it possible that the PLA's operational acts or other activities sometimes unintentionally create situations that cause difficulty for PRC foreign relations? Yes.
- Have there been instances in which some elements of the PLA have intentionally attempted to change the facts on the ground in order to influence policy? Probably yes, although we can only cite anecdotes in one or two instances that cannot be corroborated.

So is the PLA a rogue actor? No. But does the PLA sometimes exhibit roguish behaviour? Yes. The difference between the two is subtle but significant.

Big trends in elite dynamics, policy-making and national security

The major parameters of the dynamic between the PLA and the Party in national security affairs under Xi Jinping are going to be conditioned by some of the larger trends that have been at play since at least the late 1990s under Jiang Zemin and that have become much more pronounced since the 16th Party Congress in 2002 and throughout the Hu Jintao decade. At the moment, there is little reason to believe that there will be a significant break with the trends already in motion.

What, then, are some of the larger trends in Chinese elite rule in general, within the PLA, and in Chinese national security affairs that will likely persist and condition the relationship between the Party and the army under Xi Jinping's leadership? There are six worth underscoring.

First: The diffusion of authority in China. There has been no paramount leader in China since Deng Xiaoping. Certainly, as we look back across the Hu Jintao era, it becomes clear that China is now ruled by a collective leadership that is exercised by the members of the Politburo Standing Committee (PBSC)—currently seven men. The PBSC, in turn, seeks to achieve consensus on important issues; with each PBSC member having a functional portfolio as well sitting atop large functional bureaucracies that are associated with those portfolios. The CCP General Secretary is responsible, amongst some other key issues, for the military- and foreign-policy portfolios. Significantly, the uniformed PLA has no representation on this all-important body and its interests and views are channelled via the civilian Chairman of the Central Military Commission (CMC), currently Xi Jinping. This system has resulted in various bureaucracies acting at times like interest groups to have their policy preferences considered. This is no less true for the PLA.

Second: Generational change and functional specialisation. Not only are there no longer strong leaders in China, but there are no longer leaders who have impeccable *bona fides* and credible experiences across the Party, PLA, and state bureaucracies (*xitong*), which are the three pillars of the Chinese Party-state. Again, Deng Xiaoping was the last leader who could claim such attributes. Today's elite civilian Party leaders may have been exposed to the PLA throughout their careers as local officials, but they have no professional experience with military matters. Likewise, today's national-level PLA leaders, while undoubtedly exposed to civil issues while serving as local commanders, have no credible expertise in matters of civilian governance or some of the most pressing socio-economic challenges facing the new CCP leadership. Consequently, civilian Party elite and military Party elite tend to operate well within the boundaries of their functional "lanes in the road", staying out of each other's affairs and relying upon and often deferring to each other for expertise.

Third: The institutionalisation of policy-making. A third trend Xi Jinping inherits is a policy-making process in which policy is formulated or carried out by Party, army or state organs based on formally assigned institutional roles, missions and responsibilities. These, in turn, are based on functional expertise. In China, personalities still matter in policy-making, as they do everywhere in the world, but not to the point where personalities can easily overturn or subvert formal bureaucratic prerogatives, as was the case during various periods of CCP history. In short, Xi inherits a system in which there has been a rectification of responsibilities and "regularisation" (*zhenghuihua*) of process.

Fourth: Poor policy coordination procedures. Progress in policy "regularisation" notwithstanding, Xi Jinping and the "fifth generation leaders" currently preside over a system in which coordination between various Party, PLA, and state entities remains challenged. While policy coordination seems to be getting better when there is a crisis or when an issue has the personal attention of leaders at the PBSC level, routine coordination still seems to have its problems, especially between the PLA and the Ministry of Foreign Affairs (MFA). Indeed, the PRC policy coordination process has been described by some officials involved in it as hampered by stove-piped information, turf-conscious bureaucracies and poor horizontal communication. As one PRC official admitted, "We understand and are worried that the capacity of the Chinese government to coordinate foreign policy and national security decisions is weak".

Fifth: PLA professionalisation. As CMC Chairman Xi Jinping, on behalf of the Party, will exercise command over the most institutionally professional and operationally capable military ever fielded in the history of the PRC. Relative to its own past, today's PLA is a force with unprecedented pockets of operational capacity and corporate professionalism; the results of nearly two decades of focussed and funded modernisation and institutional reform. Especially since 1998, when the Party directed the PLA to divest its significant number of commercial and corporate sideline activities, the Chinese military has for the most part remained narrowly and intensely focussed on its primary mission, which is modernising and training to be able to defend and secure Chinese national interests.

Sixth: Evolving views of what constitutes a national security interest. A final trend that has affected the evolution of elite civil-military dynamics, and the role of the PLA in national security policy-making, is the broadening of Beijing's conception of what constitutes an external national security interest. The Hu Jintao decade witnessed the unprecedented globalisation of Chinese national interests. A China with a globalised economy has become a China with global political equities and, of relevance to the PLA, a China with increasing global security interests. In 2004, in recognition of this new reality, Hu Jintao issued to the PLA the "*Historic Missions of Our Army for the New Period of the New Century*". In so doing, Hu expanded the PLA's mission. In addition to its traditional missions of defending the Party, guaranteeing homeland security and safeguarding Chinese sovereignty, the PLA was enjoined to defend China's *interests*. Significantly, whereas the mission to defend Chinese sovereignty is tied to geography, the defence of Chinese interests is not. The PLA Navy's deployment to the Gulf of Aden since 2008 for anti-piracy operations is a prime example of this new viewpoint.[6]

What are the implications of these trends?

Given the intersection of the preceding six major trends, what can we, and Xi Jinping, expect to see in the dynamics between civilian and military Party elite, the role of the PLA in domestic, national security and foreign-policy making? Also, what are some of the challenges ahead?

First, the PLA's role in domestic policy will remain limited. Its role in domestic affairs has contracted over the years and has never been more circumscribed than it is today.

PLA leaders currently have little or no role in making significant decisions about domestic issues in China. This is a far cry from the military's high profile in domestic affairs during the first years of the PRC and during various stages of the Cultural Revolution (1966-1976); it is also vastly different from the role of PLA elite in supporting the return of Deng Xiaoping and his domestic agenda starting in the mid-1970s.

The very fact that the uniformed PLA has no representation on the Politburo Standing Committee underscores that China's uniformed military leaders will not sit at the pinnacle of power in China or take part in decision-making on the wide range of domestic issues that concern the CCP's top-tier elite. The limited role of the PLA in domestic affairs is further underscored by their sparse representation on standing Leading Small Groups (LSGs, lingdao xiaozu). Of the estimated dozen standing LSGs that advise and coordinate on key policy issues, the PLA has seats on only three or four that we know of; and these are mostly concerned with national security, foreign affairs, and Taiwan.[7] [The PLA undoubtedly has membership on *ad hoc* small groups that deal with security affairs, such as the maritime policy small group that was allegedly established last year.] The overall message then conveyed is that the military has scant institutional influence on most domestic issues.[8]

However, and of tremendous significance, the PLA under Xi Jinping will continue to maintain an institutional monopoly on military and defence issues.

There are two significant implications of the PLA's monopoly on all things military in China. First, this means the PLA will continue to have wide latitude in managing its own affairs "in the name of the CCP". Second, the civilian leadership will be dependent upon the PLA for military advice.

On policies and programs that have to do with the internal organisation and management of the PLA, national military strategy, as well as most military modernisation programs, the PLA is near-autonomous in its authorities. There is no civilian oversight of the PLA's management of its own affairs save the presence of the sole civilian on the CMC, Xi Jinping, who is also General Secretary of the CCP. Based on the general guidance of the CCP, therefore, the PLA is expected to be self-regulating and self-policing.

Equally if not more significant, the civilian CCP elite are increasingly dependent upon the PLA for advice on military and defence issues. There are two key reasons for this. First, in an age in which military affairs just continue to become more complex the new generation civilian CCP elite no longer have credible military backgrounds of their own and they need PLA elite to interpret these issues for them. Second, the Party-state is set up such that only one CCP organisation is institutionally responsible for military affairs: the CMC—the full name of which is the Military Commission of the Central Committee of the Chinese Communist Party. A concomitant result of the foregoing is that civilian government officials and civilian government analysts stay out of the PLA's "lane in the road". Bottom line: there are no, or precious few, competing voices with those of the PLA when it comes to military issues—especially internal military affairs and often external military developments.

On larger issues of national security or foreign policy that touch on military considerations, the PLA will have a seat at the policy-making table, and its voice will be audible. However, the PLA's views will not necessarily be more decisive than others.

In this regard, the PLA, like other Party-state bureaucracies, will sometimes take on the attributes of an interest group competing for access to and influence with the top CCP leadership. The PLA will enjoy some advantages as a lobbying institution on policy issues that matter to them. Probably the most important advantage the PLA will enjoy is excellent access to the CCP General Secretary; better access to Xi Jinping relative to organisations under the State Council, such as the MFA. This is where the CMC's status as a Party organisation provides bureaucratic advantage.

The two uniformed CMC Vice Chairmen will serve as the conduits by which the PLA will offer Xi their best policy advice. It is unclear what personal dynamics currently exist between Xi Jinping and Generals Fan Changlong and Xu Qiliang, the new CMC Vice Chairmen. Nevertheless, anecdotes from the Hu Jintao era are instructive. It was said that when either of Hu's two CMC Vice Chairmen called him, Hu Jintao was sure to pick up the phone. The bottom line is that, in bureaucracies, good access is a precondition for influence, and the PLA should have good access on issues directly in their "lane in the road" as well as for issues that touch on PLA equities.

In addition to the *gravitas* of the CMC and its uniformed members, other ways in which the PLA can make its case in policy deliberations include:

- The seats the PLA is allocated on the key LSGs that deal with national security and foreign affairs;
- PLA representation on bodies such as the Politburo (two seats out of 25), the Central Committee, the National People's Congress and the Chinese People's Political Consultative Congress;
- Internal policy papers and intelligence analyses sent to Xi Jinping and the PBSC through the CMC;
- In-person briefings to CCP leaders and appearances as subject matter experts at "Politburo Standing Committee Study Sessions";
- The potential of the PLA's large media complex to message or attempt to shape or affect the views of the top CCP leadership, other Party-state bureaucracies, and the general public; and
- The relatively recent phenomenon of some PLA-affiliated personages appearing in the Chinese (non-PLA controlled) media as policy advocates in the public domain.[9]

While the PLA has many tools with which to lobby its case it is not a foregone conclusion that its views will carry the day on issues that are not strictly military in nature. As one interlocutor once put it, "the PLA advises but the Party decides".

The PLA will contribute to, but not be the sole cause of, the challenges the Chinese Party-state will continue to face in coordinating some of its defence, national security, and foreign policies.

The PLA cannot be blamed entirely for the challenges the Chinese Party-state and Xi will likely continue to face in coordinating national security and foreign policies across relevant Party, army and state bureaucracies. Very simplistically, the root cause of the problem is the lack of a national-level coordinating mechanism short of issues reaching the leadership of the Politburo Standing Committee.[10] LSGs seem to have limited utility and special coordinating groups are *ad hoc* and ephemeral. Frankly, one can only hope that looking into this state of affairs will be on Xi Jinping's "to do" list. Nevertheless, the PLA sometimes contributes to this problem in two ways: by way of attitude and by way of its own internal coordination challenges.

On the issue of attitude, anecdotal evidence suggests that the PLA bristles at the notion that some of its activities need to be pre-coordinated with state entities such as the MFA, especially its operational activities and if such coordination is construed as asking for permission. These attitudes are reinforced by the systemic reality that, in the Party-state, the military constitutes a very insular bureaucracy with few standing horizontal linkages across the Party-state. The PLA is parallel to, not subordinated under, the State Council. As stated by one PLA interlocutor, "The PLA operates in its own sphere". Indeed, the CMC, which is a Party organisation of the Central Committee, is much higher in status than the MFA. Moreover, since there are no national-level mechanisms to provide a forcing function for such coordination on a routine basis much is left to judgement, the results of which we have witnessed in the past.

As for the PLA's own internal coordination problems, anecdotes also suggest that the PLA is itself no paragon of perfect internal coordination. One is left with the impression that the PLA's operations and training communities, which sit at the top of the pecking order in the PLA hierarchy, are dismissive of the PLA's foreign affairs and intelligence communities, the latter entities being those most likely to engage in horizontal coordination with non-PLA organisations, or at least help the war-fighters think through the larger implications of operational decisions. Also, until issues reach the level of the CMC, the four general departments of the PLA are said to operate within their own stovepipes.[11]

The PLA's new operational capabilities and its expanding mission are bound to affect Party-army and PLA-state dynamics, as well as the policy process if they have not already done so.

The PLA may in fact "operate in its own sphere", as I was told by the PLA officer cited above, but the PLA's new operational capabilities and its new mission sets are increasingly touching on the equities of other parts of the Party-state with increasingly important strategic and policy ramifications. The PLA is transforming into an incipient expeditionary force. It is operating further out at sea in the maritime and aerospace domains. It is experimenting and operating in other parts of the "global commons" such as outer space and cyber space. The PLA now regularly takes part in combined exercises with foreign militaries, and it has been participating in UN peace-keeping operations for many years. The PLA Navy is now conducting real-world operations beyond China's near seas, in the Gulf of Aden. Consequently, the PLA's operational activities increasingly have strategic, political, and foreign policy implications that cannot be ignored. In short, the

PRC's expanding definitions of what constitutes a national security interest, the PLA's expanding mission sets as handed down from the Party, as well as the PLA's new operational capabilities are already blurring the lines between military policy, foreign policy and national security policy.

These new realities beg the question of whether the current relationships and coordinating arrangements between the Party, army and state bureaucracies are serving these new realities. If not, will they be adjusted? It also begs the question of how these new realities will affect the role of the CCP General Secretary. Xi Jinping (as the CCP General Secretary, new CMC Chairman and State President) is currently the single touch point where political-military issues come together. Will this mean that Xi will have to be more engaged with the PLA than Hu Jintao was rumoured to have been? These are open ended questions at this point.

Another dimension of the PLA's growing operational capabilities is that in times of crisis the PLA can now give the CCP leadership more military options than at any other time in the past. As we all know, in bureaucracies you get a seat at the decision-making table if you come with options. With tens of thousands of Chinese nationals working in some of the world's worst neighbourhoods, with China increasingly dependent upon the importation of raw materials, with maritime sovereignty disputes close to home heating up and, as mentioned earlier, with the globalisation of China's national interests, the demand signal from the Party to the PLA to provide "options" could become stronger under Xi Jinping.

The PLA and nationalism

A final issue is the influence of nationalism on the PLA. I am still thinking through this issue, but it seems to me that nationalism is an issue that cuts two ways with the PLA. On the one hand, the PLA is one of the institutions in China that generates a certain amount of popular nationalism. I think it is important to remember that the PLA is a keeper of the flame of the PRC's national narrative. It is important to remember that the founding of the PRC and the founding of the PLA are nearly inseparable, and that, as in America, where there was a United States Army before there was a United States, in China there was a "Red Army" before there was a "Red China". The PLA promulgates the national narrative both within the PLA itself and amongst the general population through a large propaganda complex comprised of books, magazines, newspapers, television air time, CCP-sanctioned national defence education programs for students and a political work system that operates within the PLA but that touches the civilian population as well. The national narrative the Party and PLA promulgate is very simple and straightforward:

> *China was a perpetual victim due to its own backwardness in the face of foreign aggression. The CCP and the PLA restored China's dignity. China will never forget the hundred years of humiliation and will brook no challenges to its sovereignty.*

So the PLA, with the blessings of the CCP (from which it derives its major themes) has an active role in creating nationalist sentiment in China. At the same time, the PLA, like other Party and state institutions, engages in a post-Maoist version of "the mass line". They help to create the populist and nationalist demand signal, they then exclaim to foreign interlocutors that the Party and PLA must be mindful of popular nationalism when it considers policy options, especially as regards issues of sovereignty. This ought to be disturbing to many of us, as there seem to be PLA commentators in the media—though whom they represent is often unknowable—who are stoking popular nationalism as they advance provocative policies in foreign and security affairs.

Summary of key points

- Questions about the loyalty of the PLA to the Party are misplaced. The PLA remains loyal to the CCP. It does not contest the subordination of the PLA to the Party, and the PLA is probably prepared to defend the one-party rule of the CCP against challenges to the regime. It is the bureaucratic behaviour of the PLA that may be problematic, not its loyalties.

- The seemingly "roguish" behaviour of the PLA in national security and foreign policy affairs is likely more a function of systemic problems in coordinating policy and the unintended consequences of operational or other activities than of conscious acts of insubordination on the part of the military. That being said, we cannot discount the possibility that the PLA is capable of intentionally influencing policy decisions by presenting leaders with operational *faits accomplis*.

- The larger trends in elite rule in China have an impact on and determine the contours of elite civil-military relations. These trends include the diffusion of authority at the pinnacle of the political system, generational change and functional expertise, the institutionalisation of policy-making, poor policy coordination procedures, PLA professionalisation and broadening concepts of what constitutes a national interest.

- These larger trends will affect the civil-military dynamic under Xi Jinping in the following ways:

    1. The PLA's role in domestic political affairs and decision-making will continue to be constrained;

    2. But the PLA will enjoy an institutional monopoly on military and defence issues, and it will have wide latitude in managing its own affairs "in the name of the CCP";

    3. On larger issues of national security or foreign policy that touch on military considerations, the PLA will have a seat at the table, and its voice will be audible if not necessarily always decisive;

    4. The PLA will be an effective interest group, with various ways to lobby for its policy preferences;

    5. The PLA will be a party to, though not the sole cause of, the challenges the Chinese Party-state will continue to face in horizontally coordinating some of its national security and foreign policies; and

    6. The PRC's expanding definitions of what constitutes a national security interest, the PLA's expanding mission sets as handed down from the Party and the PLA's new operational capabilities are already blurring the lines between military policy, foreign policy, and national security policy for the Party-state.

Assessing the Risk of Conflict in the South China Sea

Tensions in the South China Sea have escalated in recent years as claimant parties—Brunei, China, Malaysia, Philippines, Taiwan and Vietnam—asserted their sovereignty claims over sea territory and maritime features in the region. Beyond territorial integrity, fishery and energy resources, freedom of navigation and popular support for the government are at stake. To secure these interests, the disputants have attempted to counter, deter and even initiate challenges in the contested waters. China, Vietnam and the Philippines have been the main participants of this escalatory dynamic, as seen from the confrontations near the Paracel Islands and the Scarborough Shoal stand-off. So far the involvement of the United States has had mixed results: at times US intervention has persuaded Beijing to rethink its intimidation tactics and take part in multilateral dialogue; at other times it has given China justification to act more assertively; and in some instances it has emboldened other nations to challenge China and resulted in increased tensions. It is against this troubling backdrop that this paper attempts to identify key trends in the South China Sea and factors that may escalate or mitigate tensions in the next two to three years.

Likely sources of tension

Civilian and military build-up

Development in the military and civilian patrol capabilities of the claimant states is likely to increase the probability and frequency of confrontations between claimants. China's growing fleet of paramilitary ships will further strengthen Chinese ability to pressure and intimidate its neighbours. By 2015, China will acquire 36 new marine surveillance ships in the 600-, 1000-, and 1500-tonne category[12]. This not only undergirds China's plan to conduct daily fishery patrols in the entire South China Sea in 2014, but also reflects the larger intent to establish greater paramilitary presence to strengthen and extend effective jurisdiction of its claimed areas[13]. Vietnam is also pursuing a similar strategy and has increased patrols of its exclusive economic zone (EEZ) by "maritime surveillance forces" since January 2013[14]. As claimant states exercise better and broader surveillance, more confrontations may take place in the disputed waters.

Improvements in the naval capabilities of claimant states will increase the potential for conflict and escalation. Even if the deployment of better-equipped civilian and military ships does not result in violent clashes, it may generate prolonged confrontations over disputed atolls and reefs, similar to the stand-off over Scarborough Shoal in 2012. The Philippines will receive its second Hamilton-class cutter from the US in April 2013, 10 new multi-purpose coast guard vessels from Japan in 2014 and 12 FA-50 light fighter jets from South Korea, of which two will be delivered within the next months[15]. Over the next decade, Vietnam will take delivery of six Kilo-class submarines from Russia, with the first two expected to be delivered in 2013, and will procure seven new frigates and corvettes[16]. Armed with more powerful vessels, these countries may become more willing to assert their claims (for example, by proceeding with oil or gas exploration and development in their EEZs, which are contested by China) and less willing to make the first retreat in a stand-off. They may also be further emboldened by the American "strategic pivot to Asia" which is interpreted by some claimants as suggesting that the United States will assist them to repel Chinese assertiveness.

Increasing Chinese fishing boat activity

The growing presence of Chinese fishing fleets in disputed waters over the next few years will be a latent but pervasive source of instability in the South China Sea. On one hand, this activity is motivated by economic interests: Chinese fishermen who want to meet rising consumer demand, yet faced with the problem of dwindling catches and pollution in the near seas, have little choice but to move further from Chinese shores into resource-rich waters[17]. The provincial governments of Guangdong and Hainan have abetted these forays by lowering the number of permits for small fishing vessels to promote construction of larger ships, and investing in the production of supply ships so that fishermen can remain longer in the deep seas[18]. On the other hand, it reflects the deliberate intensification of China's "salami tactics" to gradually extend its de facto control over the South China Sea. There should be little doubt that fishing and other civilian vessels have been employed as a tool of Chinese statecraft, especially after a Chinese fishing boat cut the seismic cable of a Vietnamese survey ship in December 2012. Their use will most likely intensify because of their utility: should any of these fishing boats be challenged by foreign vessels, China could choose to either exit with grace or use them as a pretext to send in reinforcements to reassert its new boundaries of control. As other claimant states repel a growing number of Chinese fishermen in disputed waters, who have travelled there on their own accord or under directions of the government, there may be more periods of heightened tensions.

Chinese efforts to extend effective jurisdiction

It is highly probable that Chinese government agencies at both the local and central levels will continue to adopt substantive measures in an effort to strengthen China's sovereignty claims on the ground[19]. One such example was the establishment in July 2012 of Sansha City, with a prefecture-level municipal government and plans for a military garrison[20]. The 18th Party Congress Political Report, which calls for China to "enhance our capacity for exploiting marine resources, develop the marine economy, protect the marine ecological environment, resolutely safeguard China's maritime rights and interests and build China into a maritime power", is likely to prompt further steps to bolster Chinese presence and influence throughout the South China Sea. Some plans are already underway.

At the central level, China's State Oceanic Administration has announced it will commence the 2nd Chinese Comprehensive Survey of Marine and Island Resources in the first half of 2013. Scheduled for completion in December 2016, this effort aims to understand the distribution, quantity and quality of marine resources and potential for exploitation" and "fill informational gaps in the base points and geological features of important islands such as the Sansha islands"[21]. If this project proceeds as planned, Chinese survey ships will move into the farthest reaches of China's sovereignty claims, such as the Spratly islands, to demonstrate jurisdiction. This will alarm other claimant states who view it as a sign of China's expansionism beyond the Paracels and the Macclesfield Bank islands, where China usually manoeuvres. Not only will Vietnam and the Philippines grow more vociferous in their complaints, but Malaysia may also begin to express its discontent. This will be unprecedented for Malaysia, which has maintained a low profile as a claimant party in the dispute: its reluctance to participate openly in maritime talks with the Philippines, Vietnam and Brunei in December 2012 shows that it does not want to be seen by China as a provocateur in the dispute[22]. The penetration of Chinese influence deep into the claimed territories of others will almost certainly provoke strong objections from many sides, escalating tensions which are difficult to quell.

At the local level, ongoing infrastructural works at Sansha City forebode impending escalation. The first-phase construction of the new port at Yongxing Island, which includes "a seawater desalination plant, a sewage treatment plant and a garbage collection and transfer system", will be completed by the end of 2013[23]. A new supply ship will also be built by 2014, so that materials can be transported faster to speed up development of the island[24]. These projects reflect the Chinese intent to support a larger

Chinese population at Sansha City, which is likely to comprise fishermen, tourists and workers from the oil and gas industries. Protecting these Chinese civilians will also necessitate the deployment of more paramilitary forces in the disputed waters. As such, once these facilities commence operations, Chinese presence at the disputed islands is likely to increase, and it will generate dissatisfaction among other claimant parties, and may even provoke them to undertake counter-responses to develop infrastructure on the islands that they control.

Poor coordination within the Chinese government

China's central leadership faces the challenge of aligning the actions of a myriad of local and central government agencies with its firm but measured rhetorical stance on the South China Sea. A Maritime Rights Office has reportedly been formed as a sub-unit of the Foreign Affairs Leading Small Group (LSG) to coordinate policy on the dispute[25], but like other LSGs, it is likely empowered to propose broad strategic guidance that is then endorsed by the Standing Committee of the Politburo and has no power to decide how the guidance is implemented by the agencies involved. There are also no institutionalised lines of command or rules specifying when and how government bodies can seek approval to act on matters relevant to the dispute.

Compounding this state of affairs is a weak Ministry of Foreign Affairs (MFA), whose ability to coordinate is circumscribed by its lack of authority to direct significant actors such as the People's Liberation Army[26]. The structural inability to harmonise policy becomes problematic when Chinese leaders proclaim that they aspire to build the country into a "maritime power" and will "never sacrifice core interests" yet also commit to follow the "road of peaceful development"[27]. Government bodies are likely to interpret these messages as condoning more assertive behaviour, and may initiate actions which are stronger than the official line. Yet the central leadership cannot revoke these measures without appearing weak to the Chinese public and other claimant states. Recent efforts to impose supervision, such as the need for city planning of Sansha to be approved by the State Council, reveal the problem of lack of coordination, but do not resolve it.

An enfeebled ASEAN

It remains doubtful whether ASEAN can conclude a Code of Conduct (COC) with China in the next three years, and, even if achieved, whether such an agreement would bring stability to the South China Sea. While ASEAN is keen to begin talks on the COC, China's response has been lukewarm. Beijing's position is that it will only consider discussing the COC "when the time is right" and only through bilateral consultations[28]. This likely means that other claimants must first cease and desist from actions deemed by China as provocative; the United States must reduce its involvement in the issue; and ASEAN must agree to a watered-down version of the COC that is non-binding and/or lacks dispute settlement mechanisms. It seems unlikely at present that such concessions will be made. Forcing China to appear at the negotiation table is also not feasible for ASEAN, since it lacks cohesion to exert sufficient pressure.

At the same time, the extent to which the next few ASEAN chairs can advance discussions on the Code is modest. As the Chair for 2013 and also one of the claimant parties, Brunei could make the negotiation of a binding COC a top priority, but as a small state it lacks the clout to foster consensus between China and ASEAN. Burma and Laos, the ASEAN Chair for 2014 and 2015 respectively, are both probably too economically dependent on China to nudge it into an agreement. Furthermore, the planned 2015 ASEAN integration will consume the attention and energy of these Chairs and most likely dilute efforts away from the more intractable South China Sea dispute.

Even if ASEAN and China manage to cobble together a Code within the next three years, it will probably lack the teeth to dampen seriously the risk of conflict in the disputed waters. There are deep differences to overcome: ASEAN's vision for the Code includes dispute settlement mechanisms which China wants to be replaced with confidence-building measures; there is also no agreement on what exactly constitutes the disputed areas[29]. In the absence of a robust agreement that has provisions for regulating behaviour in the South China Sea and peacefully resolving disputes as well as enforcement and dispute settlement mechanisms, all claimants will put their country's interests first, exacerbating competition and tension.

Challenging China's South China Sea claims through international arbitration

The Philippines' move to refer China's nine-dashed line claim to the South China Sea to the United Nations' arbitral tribunal introduces a legal dimension to the dispute. As expected, Beijing refused to accept international proceedings. Nevertheless, the arbitration is likely to proceed. Past cases suggest that a ruling will be handed down in three to four years. If the tribunal rules completely in favour of Manila, it could declare the nine-dashed line invalid and require removal of structures like those on

Mischief Reef, and an end to interference with Philippine fishing, energy exploration and other activities. However, the tribunal has no mechanism to enforce the ruling and China is unlikely to comply, even though its international image will be harmed if it is seen as contemptuous of international law.

In the meantime, tensions could mount if, for example, China attempts to consolidate its position and create a *fait accompli* by building new structures on Scarborough Shoal. The Philippines could seek an order for provisional measures from ITLOS to restrain Chinese activities in disputed waters, which would provide an early test of Beijing's willingness to comply.[30]

China will probably want to ensure that it is "business as usual" in the South China Sea, in spite of the legal challenge, to show that it is immune to such international pressure. It is therefore likely to continue to press its influence in the contested waters, and employ economic means to punish the Philippines as payback for internationalising the dispute. Yet, given that the arbitration process has already raised international awareness of the dispute, China will have to think twice about retaliating too strongly lest its actions generate fear among other ASEAN members that results in increased alignment and cooperation with the United States.

Brinkmanship by on-site patrol vessels

The interaction between the aforementioned variables, namely rising capabilities and weak oversight, presents the greatest risk of armed conflict in the South China Sea. As the Chinese government displays its paramilitary and military strength and continues to talk tough on the dispute, paramilitary vessels on the ground are emboldened to adopt more provocative measures, such as threatening to ram foreign vessels, knowing that the Chinese authorities can and will protect them in a potential conflict. The top leadership will find it difficult to keep these belligerent tendencies in check, as it normally does not exercise complete supervision of these personnel who operate under looser chains of command; micromanagement of Chinese vessels takes place only after the onset of crises like the Scarborough Shoal incident. Therefore, Chinese paramilitary ships run the risk of a hostile confrontation when they execute more coercive forms of manoeuvring towards "intruders", who might then misperceive them as an impending attack and fire the first shot in self-defence.

Potential stabilising factors

Influence from the ringside

Increased influence by third parties on the dispute may produce greater circumspection in Chinese behaviour. Already the Japanese administration has signified the importance of Southeast Asia to Japan, as Prime Minister Shinzo Abe and his Foreign Minister Fumio Kishida made their first foreign trip to the region. Japan has notably warmed up to the Philippines by providing coast guard vessels and pledging closer maritime cooperation[31]. The underlying intention is to prevent Southeast Asian claimant states from conceding to China, which could threaten freedom of commercial passage in the South China Sea and therefore put at risk the delivery of oil to Japan, and also encourage Beijing to toughen its stance on the Senkaku/Diaoyu Islands[32]. From the Chinese perspective, Japan's engagement strategy forebodes the unpleasant possibility that it might have to deal with concerted pressure on two fronts someday. To avert this outcome and to avoid driving other claimant states into the arms of Japan, China might exercise greater restraint in its activities in the South China Sea for the time being.

Indian interests in the South China Sea will probably lead to China acting with greater caution in parts of Vietnam's EEZ, namely in blocks 61 and 128 where the Indian petroleum company ONGC Videsh currently operates. China has little reason to assert itself there; doing so could increase the risk of Indian navy ships being deployed into the disputed waters. India appears intent to maintain a distance from the dispute, as seen from its foreign minister's rejection of Indian intervention in the South China Sea[33]. It is likely that India and China will avoid antagonising each other over this issue.

The United States can and will likely continue to play a role to prevent disputes from getting out of hand. In many circumstances, US involvement is successful in defusing tensions or promoting greater cooperation, but at times, it admittedly results in greater friction. An example of the U.S. playing a role in ameliorating tensions is China's agreement on the guidelines for the implementation of the Declaration of Conduct in 2011, which followed increased international pressure, in particular by the United States, at the 2010 ASEAN regional forum. The United States also helped defuse the Scarborough Shoal stand-off in 2012 by facilitating a deal between China and the Philippines[34]. However effective America's role might be, it is circumscribed by the need to maintain neutrality on the territorial dispute, to avoid jeopardising US-China relations and to prevent claimant states like the Philippines from being emboldened to act aggressively. This means that the United States will likely maintain its current practise of only intervening to contain tensions when they are dangerously high or working behind the scenes to promote the establishment of mechanisms, such as the Code of Conduct, that will facilitate the management or resolution of the disputes.

Depoliticising energy development

Another reassuring trend is the exercise by claimants of greater restraint over energy exploration and drilling activities in the South China Sea. In June 2012 the China National Offshore Oil Company (CNOOC) put up nine exploration blocks for bidding which were all situated in the waters claimed by Vietnam; in contrast, its subsequent offer in August only had one out of 26 blocks that was perceived by Vietnam to be in disputed waters[35]. This pull-back is in conformity with the Chinese government's position that it remains interested in joint exploration with its neighbours and seeks to depoliticise energy development.

Similarly, the Philippines delayed exploratory drilling at the Reed Bank by withholding approval for Forum Energy to proceed. Its willingness to postpone the August 2013 deadline allows for the possible inclusion of a Chinese oil company and suggests the desire to avoid provoking Beijing. However, the prospects of a partnership between CNOOC and Forum Energy to drill at the Reed Bank, which would have been a display of commercial cooperation to ease tensions, have been severely dampened by the Philippines' decision to seek international arbitration against China over its South China Sea claims. Before this a partnership seemed possible, as China's ambassador to the Philippines was in favour of such an arrangement and President Aquino was also open to the idea of joint exploration[36]. Now, however, there is little likelihood that CNOOC will join the drilling effort. It remains to be seen how Beijing will react when Manila declares that drilling in Reed Bank can proceed.

Conclusion

In sum, tensions in the South China Sea are likely to rise over the next few years due to the widespread and persistent use of "salami tactics" by Chinese civilian, bureaucratic and paramilitary actors, as well as the inability of both domestic and international institutions to moderate assertive behaviour. Confrontations may also take a longer time to subside, as stronger capabilities make the claimant parties more unwilling to initiate a retreat. Nevertheless, the influence of the United States, Japan and India, as well as the possible de-politicisation of energy development may help prevent tensions from getting out of hand. If Sino-Japanese friction in the East China Sea remains high, then Beijing may attempt to keep tensions in the South China Sea low for the time being.

Signs since the 18th Party Congress suggest that Xi Jinping supports China's existing strategy in the South China Sea of more assertively pressing China's claims and seizing opportunities when presented to alter the *status quo* in China's favour, as was achieved in the case of the dispute with the Philippines over the Scarborough Shoal. In Xi's January 2013 inaugural foreign policy address to a Politburo study group, he stated bluntly that "No foreign country should ever presume that we will bargain over our core national interests"[37]. The contradiction between China's commitment to "rise peacefully" and to "defend its sovereignty and territorial integrity" at all costs is likely to persist.

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Economic and Geo-Political Implications of China-centric Globalisation

China-centric globalisation

The last thirty years have witnessed the era of globalisation which can be defined as the creation of an integrated global economy. However, what began as a project for globalisation has gradually been transformed into a project of "China-centric globalisation". This paper argues that China-centric globalisation has grave economic and geo-political implications for the US. It also carries major implications for other countries, although those implications obviously vary according to country-specific economic and political details.

China-centric globalisation is characterised by three features: 1) the emergence of China as the global centre of manufacturing—the so-called "factory for the world"; 2) the creation of a new dollar zone shared by the US and China, and supported by China's adoption of a pegged dollar exchange rate; and 3) the emergence of a massive US trade deficit with China, combined with the transfer of a significant chunk of US manufacturing capacity to China.

China-centric globalisation is an extension and evolution of corporate globalisation, which in turn evolved out of the post-World War II free trade era. This evolution is visible in US trade statistics shown in Table 1. Stage 1 of this evolutionary process ran from 1945 to 1980 and constituted the "free trade" era. It was characterised by rising trade openness, measured by goods exports and imports as a share of GDP, with roughly balanced trade. Stage 2 ran from 1980 to 2000 and constituted the era of corporate globalisation which was marked by a continuing rise of trade openness, but now with rising goods trade deficits as a share of GDP. Stage 3 has run from 2000 to present and constitutes the era of China-centric globalisation. It has generated a continuing rise in the goods trade deficit as a share of GDP plus an increase in the share of US imports from China.

Table 1. U.S. trade statistics and the emergence of China-centric globalization
(X = goods exports, M = goods imports, GDP = gross domestic product).

	[X+M]/ GDP	[X-M]/ GDP	China X/ X	China M/ M	China [X-M]/[X-M
1960	6.7%	0.1%			
1980	17.0%	-0.1%	1.8%	0.1%	N.A.
2000	20.2%	-4.5%	2.0%	8.1%	18.8%
2010	22.0%	-4.4%	7.1%	18.8%	42.2%

Source: Economic Report of the President, Congressional Research Service,Census Bureau and author's calculations.

Globalisation was always problematic for both national security and national shared economic prosperity. China-centric globalisation makes it more so. Why? First, it aggravates the impacts of globalisation on both national security and shared prosperity. Second, it constrains US economic policy space. Thus, it has hindered US attempts to escape the Great Recession by limiting capacity to address the trade deficit via exchange rate adjustment; it also promises to block any future attempts to recalibrate globalisation so as to make it more equitable and environmentally sustainable.

Manufacturing and economic security

The conventional focus of concern has been China's effect on manufacturing and economic security. This concern is now widely acknowledged and discussed. The basic story is China-centric globalisation has caused large transfers of technology and manufacturing capacity to China; shrunken the US manufacturing base; promoted enormous financial investments in China; and caused the emergence of a huge trade deficit that has cumulated into making China the largest foreign holder of US government debt. These developments pose both economic and national security dangers. A shrivelled manufacturing base promises lower future productivity growth and exposes the US to potential balance-of-payments constraints. It also undermines national security because reliance on imported manufacturing goods could undermine the ability to equip a modern military and fight a lengthy war. A related concern is off-shoring of industrial research and development (R&D) facilities to China as the location of R&D seems to follow the factory. That will reduce the flow of future innovations. Since power is relative, the above developments strengthen China by strengthening its manufacturing base, its export prowess, its R&D capacity and its capacity to sustain a modern military.

Financial security

Another issue that has received some attention is that of financial security. Here, the argument is that persistent large trade deficits have meant China has accumulated massive financial claims against the US, making it the largest official creditor of the US. The fear is that this debt gives China power and leverage over US financial markets. In the event of tensions, China could disrupt US financial markets using strategic selling that spikes interest rates and damages the US economy. A classic example of vulnerability to financial pressure is provided by the 1956 Suez crisis when the US threatened to financially undercut Britain and France if they did not end their occupation of the Suez Canal.

However, these financial security fears are easily overstated. US debts are dollar-denominated so the Federal Reserve can always step in and buy them, as it has done with its quantitative easing program (this was not the case for Britain in 1956 which had borrowed dollars). The US Treasury also has the power to freeze holdings. Lastly, massive selling of assets would impose financial losses on China and that is a deterrent to doing so.

Geopolitical security

Whereas significant attention has been directed to the issues of manufacturing and financial security, much less attention has been directed to the issue of geopolitical security. Here, China-centric globalisation has major ramifications that implicate every region of the globe (East Asia, Africa, Australia, Latin America and Europe), and these implications appear to be little appreciated.

The key feature is that the post-Cold War world is marked by a new form of geopolitical competition. In the Cold war era, the currency of competition revolved around military force and ideology. In the new era, the currency of competition is economic power that fashions durable commercial alliances. China-centric globalisation gives China economic and financial power to build these alliances, while it also undermines US economic and financial power. That combination dramatically weakens US geopolitical power and security.

China's geopolitical financial challenge

In addition to the financial security threat, China-centric globalisation also creates a geopolitical financial challenge. First, China's financial wealth gives it increased power in multilateral institutions like the International Monetary Fund (IMF) and World Bank. It also gives China financial power to woo domestic elites, a power that was recently on display in Canada with China's purchase of the energy firm, Nexen. Regardless of the economic merits of that transaction, it showed China's capacity to deploy financial resources and affect domestic politics by exploiting differences of interest within Canada. Second, it gives China increased geopolitical influence and power thanks to its ability to grant credit and foreign aid. This increased power is not just vis-à-vis developing countries. It also affects developed economies, as evidenced in China's courtship of countries affected by the euro crisis, particularly Greece.

East Asia and the global supply chain

China-centric globalisation has also dramatically impacted US geopolitical standing in East Asia. Here, the critical change has been the restructuring of the global supply chain.

Globalisation has always raised supply chain security concerns because sourcing from outside one's borders is intrinsically more dangerous. The traditional threat metrics consist of the vulnerability of the foreign supply chain (distance); the extent of foreign supplier diversification (the number of supplier countries); and the extent of quantitative reliance on foreign suppliers (imports as a share of manufacturing output). Greater distance, fewer supplier countries and greater quantitative reliance all increase the potential national security threat.

China-centric globalisation has increased this threat by making the US global supply chain more vulnerable to interruption and more dependent on China. This is illustrated in Figures 1 and 2. Figure 1 contains a stylised illustration of the global supply chain that, in the 1980s, had the US supplied by many East Asian countries (eg. Japan and South Korea). This exposed the US to dangers of distance, but the supply chain was relatively well diversified and the level of quantitative dependence was also low. Figure 2 shows the new supply chain that places China at the centre in a role as product assembler. China receives inputs from East Asian suppliers, assembles them, and then ships the finished goods to the US. This middleman position gives China increased leverage.

Figure 1. Stylised representation of the 1980s global supply chain.

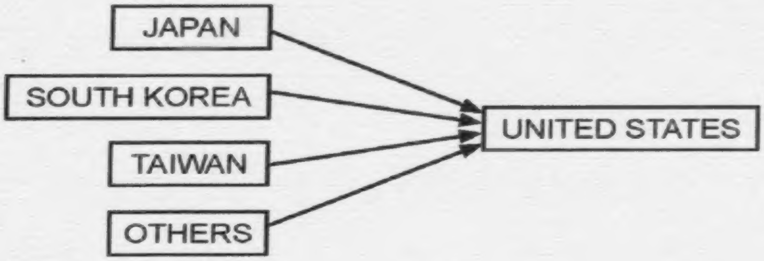
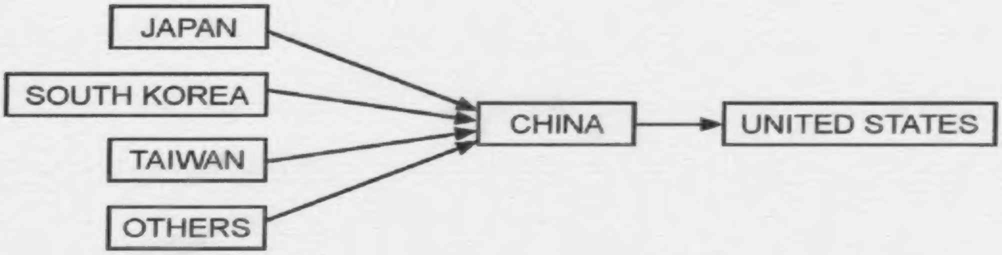


Figure 2. Stylised representation of the 2000s China-centric global supply chain.



It also makes East Asian countries more dependent on China which increases China's regional power. Moreover, it projects China as the engine of regional economic growth, for which China gets significant diplomatic credit, when in fact the US is the ultimate engine since demand for East Asian inputs is derived from US demand for Chinese assembled products.

China's resource diplomacy in Africa, Latin America and Australia

China-centric globalisation has also considerably increased China's geopolitical power with regions exporting natural resource. The basic logic is that by making China the factory of the world, it has created the basis for new commercial alliances. The economic logic of these alliances is China exports manufactures to these countries and in return receives imports of natural resources.

In the Cold War, the Soviet Union could never accomplish that because it was a resource exporter and was in competition with these countries. Consequently, the Soviet Union had little to offer economically; instead, it offered guns and ideology. The US used to be the supplier of goods and buyer of resources but, as its manufacturing base has shrunk, it has been increasingly displaced by China. That places the US in a weaker position versus China than it was versus the Soviet Union.

Resource exporters have benefitted from China's rise thanks to the increasing prices of raw material and access to cheaper manufactured goods, as well as from Chinese foreign direct investment (FDI). But they also suffer. First, China is undemocratic and its commercial practises promote the "natural resource curse" as it tolerates corruption and violations of human rights and labour standards, which harm development. Second, China's mercantilist commercial policy and undervalued exchange rate undermine manufacturing development in these economies. Third, higher resource prices are not a "free lunch" as they promote exchange rate appreciation that drives deindustrialisation—the so-called Dutch disease. The bottom line is the new relationship between China and resource exporters has inexorable commercial logic but it is not necessarily good for development.

The trans-Atlantic relationship between the US and Europe

Lastly, China-centric globalisation also has implications for the trans-Atlantic relationship with Europe which has been the bedrock of the international system after World War II. The structure of global production under China-centric globalisation exerts a tendency to pull the US and Europe apart by creating rivalries between them.

As mentioned above, China has already used its financial strength to woo Europe during the current euro crisis. Second, with regards to trade, there has been some decline in the significance of trade with Europe for the US as measured by the size of total trade with Europe relative to GDP. Third, and most importantly, the new economic structure tends to create a "prisoner's dilemma" situation between the US and Europe. The two would do best by cooperating in their dealings with China, but the structure of China-centric globalisation has them engaging in mutually injurious competition that benefits China.

This is particularly evident in the aircraft industry in the competition between Boeing and Airbus. China has been able to use its state control over purchasing by Chinese airlines to manipulate Boeing and Airbus into patterns of disadvantageous competition. These patterns include forced technology transfer and shifts of manufacturing and assembly to China. That has cost jobs and investment; it threatens the long-term prosperity of both of these key companies by potentially creating a commercial rival.

> *China has been able to use its state control over purchasing by Chinese airlines to manipulate Boeing and Airbus into patterns of disadvantageous competition.*

Trouble ahead

China-centric globalisation is very problematic for the US from both economic and geopolitical standpoints. The problems are not going away and promise to get worse. The trade deficit, investment diversion and exchange rate policy have already hindered US economic recovery from the

Great Recession of 2007-09. China's mercantilist export-led growth model poses a threat to global development because other countries are now unable to get on the ladder of manufacturing. Lastly, the US push for a flexible renminbi with open capital markets to resolve the exchange rate question is particularly misguided. If implemented, a flexible renminbi risks exposing the US to renminbi depreciation as it is quite likely there will be future capital flight from China. That is because Chinese wealth holders are undiversified internationally and they are also subject to domestic political risk. Furthermore, there is the possibility of a Chinese economic bust.

Conclusion

China-centric globalisation raises clear concerns. Despite that, it has been very hard to get discussion on the policy table. There are several reasons for this. First, and foremost, is the fact that many large corporations have benefitted from China-centric globalisation and they control international economic policy discourse in Washington. As significant beneficiaries from China-centric globalisation, they block any challenge. That speaks to a grave weakness in the US political system. Corporations have become the most powerful political actors but their goal of global profit maximisation is different from the goal of advancing the national interest.

Second, there is little understanding of the distinction between globalisation and China-centric globalisation. That fosters the misunderstanding that rolling back China-centric globalisation is synonymous with rolling back globalisation. Third, globalisation (which includes China-centric globalisation) creates "lock-in" whereby economic arrangements are difficult to reverse except at considerable cost. That cost discourages change.

Finally, there is a conceit that there are no security dangers because economic links with China will turn China into a democracy and democracies do not go to war with each other. That conceit is very dangerous as evidenced by the history of the late 19th century when there was a seismic shift in relations between Great Britain and Germany that ultimately led to World War I. Britain and Germany had monarchs who shared a common lineage, yet they still went to war. The US and China are not close allies, have many areas of competition and have different political systems. That speaks to the dangers of China-centric globalisation which has been allowed to develop with great rapidity and little public discussion of its implications and consequences.

Chinese Acquisitions of Canadian Companies and Chinese Greenfield Investments in Canada: When are there Genuine National Security Threats?

This paper addresses two interrelated issues of central interest to Canada as Chinese outward foreign direct investment (FDI) grows to be a major force in the international economy. First, what is the impact of Chinese FDI on the structure of natural-resource industries around the globe? Does Chinese FDI "lock up" production of minerals, oil and gas in an exclusive manner that deprives non-Chinese users from the world supply base? Second, when does Chinese FDI via acquisition of an existing Canadian firm, or any external acquisition of an existing firm anywhere, constitute a legitimate national security threat to the home country where the proposed acquisition is headquartered? Is the national security calculus different in cases of inward Chinese greenfield investment?

Chinese lock-up of the world natural resource base?

Beginning with the first issue, are the growing number of Chinese natural resource investments taking over the global resource base with zero-sum implications for others? When Chinese companies take an equity stake in central Asian oil fields, extend loans to mining and petroleum investors in Africa, write long-term procurement contracts for minerals in Australia, or propose to acquire natural resource companies headquartered in Canada, do these activities cut off other buyers from access to world supply? Or, might Chinese investments, loans, and long-term contracts constitute a positive influence for non-Chinese buyers, helping to multiply suppliers and expand access to the world resource base?

The Chinese deployment of capital to procure natural resources takes four forms:

- In the *first procurement arrangement*, Chinese investors take an equity stake in a very large already-established producer so as to secure an equity-share of production on terms comparable to other co-owners.

- In the *second procurement arrangement*, Chinese investors take an equity stake in an up-and-coming producer so as to secure an equity-share of production on terms comparable to other co-owners.

- In the *third procurement arrangement*, Chinese buyers and/or the

Chinese government make a loan to a very large already-established producer in return for a purchase agreement to service the loan.

- In the *fourth procurement arrangement*, Chinese buyers and/or the Chinese government make a loan to finance an up-and-coming producer in return for a purchase agreement to service the loan.

These four structures provide the basis for examining the potential to "tie up" supplies. If the procurement arrangement simply solidifies legal claim to a portion of the output of established large producers (first and third structures), this gaining "preferential access" to supplies does have exclusionary implications for other consumers. In contrast, however, if the procurement arrangement expands and diversifies sources of output more rapidly than growth in world demand (second and fourth structures), the zero-sum exclusionary implication does not hold because other consumers have easier access to a larger and more competitive global resource base.

An assessment of the sixteen largest Chinese natural resource procurement arrangements around the world reveals the predominant pattern (thirteen of sixteen projects) is to take equity stakes and/or write long-term procurement contracts with the competitive fringe. A brief review of four smaller Chinese procurement arrangements—undertaken to check for selection bias—shows only one that has zero-sum implications for other buyers. A comprehensive examination of the universe of thirty-five Chinese natural resource investments and procurement arrangements in Latin America indicates that twenty-three help diversify and make more competitive the portion of the world natural-resource base located in Latin America. Thus widespread apprehensions about Chinese potential to "lock up" of world resources are *not* supported by this hypothesis. (As discussed later, Chinese manipulation of rare earths resources constitutes a notable exception.)

Upon reflection, such behaviour on the part of China should not be surprising; in comparative perspective, the Japanese government, for example, considered a strategy of pushing the country's own major "national champion" resource companies to establish relationships with major OPEC members and other extractive-intensive countries to exercise control over a portion of world supplies. From the late 1970s through the 1980s, however, Japanese policies shifted towards procurement arrangements that would make the structure of global extractive industries more competitive and diversify the geography of production, a strategy that is maintained by Japanese investors today.

The impact of Chinese procurement arrangements on the structure of natural-resource industries around the world is by no means the only object of concern; indeed this competitive outcome is *only one dimension* of the geopolitical challenges surrounding Chinese investment behaviour. It must be noted that Chinese natural-resource investment flows to problematic states and regions, including Iran, Sudan and pre-reform Myanmar. In addition, Chinese investors often expose host countries in the developing "resource curse" practises of illicit payments, graft and corruption, as well as poor worker treatment and lax environmental standards.

In addition, it is important to note that not all Chinese strategic manoeuvres towards natural resource procurement reflect the predominant trend towards making the supplier base more competitive. Chinese policies to exercise control over "rare earth" mining runs precisely in the opposite direction, a fact that will feature prominently in any proposed Chinese acquisition of rare earth firms in Canada or in already concentrated resource industries in general (such as potash).

Identifying national security threats from foreign investment: separating plausible from implausible outcomes

Turning to the second issue of interest for this paper—establishing a framework for distinguishing genuine national security threats from implausible assertions of such threats—a comparative review for a Canadian audience of US foreign acquisition cases reveals three kinds of threat. The first category of threat ("Threat I") is that the proposed acquisition would make the home country dependent upon a foreign-controlled supplier of goods or services crucial to the functioning of the home economy that might delay, deny or place conditions upon provision of those goods or services. The second category of threat ("Threat II") is that the proposed acquisition would allow transfer of technology or other expertise to a foreign-controlled entity that might be deployed by the entity or its government in a manner harmful to home country national interests. The third category of threat ("Threat III") is that the proposed acquisition would allow insertion of some potential capability for infiltration, surveillance, or sabotage, using a human agent or some non-human mechanism, into the provision of goods or services crucial to the functioning of the home economy.

Potential national security threats from inward, greenfield investments will be considered later. For any of these three threats to be credible, the industry in which the proposed acquisition would take place must be tightly concentrated, the number of close substitutes limited and the switching costs high. Might Lenovo's proposal to acquire IBM's PC business, for example, pose a credible national security threat to the home country of the target company? Looking at Threat I (denial) and Threat II (leakage of sensitive technology), competition amongst personal computer producers, for example, is sufficiently intense that basic production technology is considered "commoditised". It is exaggerated to think that Lenovo's acquisition of IBM's PC business could have represented a "leakage" of sensitive technology or provided China with military-application or dual-use capabilities that are not readily available elsewhere. Nor could Lenovo manipulate access to PC supplies in any way that would matter. As for Threat III (infiltration, espionage, and disruption), any purchasers that feared bugs or surveillance devices within Lenovo PCs could eschew Lenovo and simply purchase any one of numerous alternatives.

Applying the three-threats framework to foreign acquisitions of Canadian companies

This three-threat framework appears to fit Canadian needs quite appropriately, beginning with potential foreign acquisitions of Canadian companies in the extractive sector. While a complete analysis of the evolving structure of the international fertiliser industry is not attempted here, the evidence suggests that supplies of both potash and phosphates are becoming more concentrated (with the former centred in Canada and the latter centered in Morocco) as US sources diminish. Within this context, BHP Billiton's hostile bid for Potash Corporation of Saskatchewan would fall into the category of placing external control of a major world source of supply into foreign hands rather than in the category of helping to expand, diversify and make more competitive the world supplier base. How BHP Billiton exercised control over output levels, prices and destination of sales could become problematic for Canada, even though provincial and national authorities could take steps to try to influence BHP Billiton's actions post-acquisition.

There was public discussion at the time of the BHP Billiton bid for Potash Corporation that a Chinese or even a Russian firm might be an alternative to BHP. From a national security point of view, neither of these alternative acquirers would be preferable to BHP, since each of these too would represent transferring external control of a major world source of supply in an increasingly concentrated industry to an external actor. Thus it is important to note how the national security framework introduced here differs fundamentally from the consideration of economic "net benefit", as contained in the *Investment Canada Act*. In the Potash case, a Chinese or Russian acquirer might offer a higher price to shareholders than BHP Billiton or make more generous no-layoffs commitments. However, this would not alter the calculation in the national security calculus: concern about transferring external control of a major world source of supply in an increasingly concentrated industry to an external actor would remain. (A quick review of the concentrated structure of the international nickel industry suggests that the proposed acquisition of Noranda by China Minmetals in 2004, never consummated, should also have qualified for national security assessment rather than a simple "net benefit" calculation.)

Potential acquisitions of Canadian rare earth elements (REE) companies might be subjected to the same calculus as Potash. A hypothetical Chinese acquisition of Avalon Rare Metals or Great Western Minerals Group would further consolidate Chinese control over the global REE industry. Indeed, Canadian authorities might want to be concerned about such consolidation even if a proposed Chinese acquisition did not involve a production site on Canadian soil. Again as a purely hypothetical example, a proposed Chinese acquisition of Great Western Minerals Group's operations at Steenkampskraal in South Africa would qualify to be blocked by Canada on national security grounds. Indeed, even a greenfield investment by a Chinese company over undeveloped REE sites in Canada would serve to extend tight Chinese control over the industry.

The above example highlights the important observation that review within the national security framework presented here requires considerations beyond what might ordinarily be contained in a typical anti-trust review of a potential acquisition. Canadian authorities would want to be cognizant of Chinese government manipulation of rare earth exports to Japan as part of geo-strategic rivalries in North Asia—and make a judgement about the advisability of permitting a hypothetical Steenkampskraal acquisition in light of Canadian foreign policy considerations—rather than looking solely at anti-competitive outcomes in a purely economic sense. In this sense, national security reviews could draw on widely accepted industry concentration measurements but would have to add more explicit considerations of Canadian national interest.

In contrast to the Potash case, the decision of PetroChina to exercise its option to acquire the entire undeveloped MacKay River project from Athabasca and Sinopec's acquisition of new drilling lands owned by Calgary-based Day Energy would appear, to the outside observer, to be helping to expand and diversify Canada's energy base. So would the China

National Offshore Oil Company's (CNOOC) acquisition of Nexen; so would Petronas's acquisition of Progress Energy; so would hypothetical greenfield investments in Canadian energy projects on the part of external investors.

The national security framework presented here can be used to evaluate foreign acquisitions outside of the natural resource sector, such as the proposed purchase of the space technology division of Vancouver-based MacDonald, Dettwiler and Associates (MDA) to Alliant Techsystems Inc. (ATK) of the United States in 2008. From a national security point of view, the proposed sale would transfer control of Radarsat-2, a high-resolution satellite with a particular kind of polar orbit, to ATK. Alliant promised to honour all of MDA's outstanding contracts with the government of Canada, including access protocols to Radarsat-2 for surveillance of the Arctic. However, Alliant could not ensure that the US government would refrain from imposing controls on Canadian access to information if there were a dispute between the United States and Canada about sovereignty in the Arctic. The United States does not recognise Canada's designation the Northwest Passage shipping channel, for example, and might refuse to permit Canada to use Radarsat-2 surveillance to enforce its claim. Given the unique nature of Radarsat-2's technology and polar orbit, what has been labelled "Threat I" earlier would come into play since Canada would have no other alternative if the US were to behave so.

This paper does not presume to assess the merits of a possible US-Canada dispute over Arctic sovereignty, but within the framework proposed here an argument for rejecting the proposed acquisition for Canadian national security reasons ("Threat I") does not appear inappropriate.

This brief review of how the national security threat assessment apparatus introduced in this paper might be applicable to sensitive cases in Canada should be coupled with a clear statement about the principal value of using such a rigorous framework—namely, to show that the vast majority of proposed foreign acquisitions will *not pose any plausible threat whatsoever*. Application of this framework in Canada should, as elsewhere, help dampen down politicisation of individual cases and lead to swift and confident approval of those acquisitions where genuine national security threats are totally absent.

Industrial Upgrading in China: Moving in the Right Direction?

China's manufacturing sector has played an important role in the economy's growth in the last three decades, expanding at a rate nearly at par with the rest of the economy. Currently, manufacturing contributes upwards of 35 percent of gross domestic product (GDP) and is the source of nearly 90 percent of its exports. Despite the massive lay-offs from the state manufacturing sector beginning in the mid-1990s, manufacturing has continued to absorb new workers, and in 2010 manufacturing activity accounted for over 110-120 million jobs.[38]

Concerned about manufacturing's future prospects, recent policy initiatives of the central government including the 12th Five-Year Plan for Science and Industry, and the Five-Year Plan for National Strategic Emerging Industries are calling for new national industrial upgrading efforts. These efforts are predicated on a view of only limited upgrading and development of innovative capacity, especially in "Chinese" firms, and the reported dominant role of the extensive margin, ie. increases in labour and capital—and not productivity growth—as the key source of growth in the Chinese economy.[39] These views, as well as nationalist and strategic concerns, are playing into China's current big push for "indigenous" innovation and the development of ambitious plans in priority areas extending from energy resources to biotechnology to IT—initiatives that often envisage restricted roles for multinationals. As part of these efforts, the Chinese government is also promoting a big outward push by domestic firms.

The perception of limited upgrading in China's manufacturing may be off the mark, however. So may be the government's assessment of the critical constraints on upgrading and innovation by Chinese firms, as well as the kinds of policies and investments it is promoting most likely to foster new innovation[40]. Both have potentially important implications looking forward. Recent research[41] points to impressive growth in productivity in Chinese manufacturing in the last decade and a half that is comparable or higher than rates observed in Japan, Taiwan or Korea over similar extended periods in their development. This growth is relatively broad based and cuts across sectors, regions and ownership groups. There has been a striking narrowing of the productivity gap between state-owned and foreign-invested firms between 1998 and 2007. Product upgrading in the form of cost *and* quality innovation that allows firms to capture rising market share in demanding international markets is also clearly evident in China's export behaviour. Exports, however, only make up a sixth of China's manufacturing output, which points to the important role of upgrading in the context of China's domestic market.

Equally telling, productivity growth is occurring less through the upgrading efforts and improvements in "continuing" or "surviving" firms, and much more because of "creative destruction" and the dynamic process of entry and exit. Between 1995 and 2010, for example, several hundred thousands of new manufacturing firms have been established, a majority of which are private. Exit has also been common. When new (old) firms enter (exit) the productivity distribution at levels higher (lower) than incumbents firms, total productivity rises; new firms also contribute positively to productivity growth subsequent to entry. Recent estimates[42] suggest that this margin may be the source of as much as sixty percent of productivity growth in manufacturing since the mid-1990s.

This perspective focusses our attention on the role of market liberalisation and the dynamics of competition in China. This process began in the early 1980s with the rise of the township and village enterprise (TVE) sector and the introduction of the dual-track system, and accelerated in the 1990s as a host of internal and external barriers came down. China did not enter WTO until 2001, but tariffs and non-tariff barriers actually experienced a much larger reduction before entry than after. Between 1992 and 2000, for example, average tariffs fell from 43 to 18 percent, and then further to 7 percent by 2010. With tariff reductions passed through almost one-for-one into lower domestic prices, the productivity threshold that entering firms must achieve in order to be profitable has been rising.

By virtue of its size and rapid per capita GDP growth, China has become the largest market in the world in a growing list of consumer and producer goods. In mobile handsets, for example, demand grew from 35 million in 2000 to 225 million in 2010, or twenty percent of global demand; in automobiles, more than 11 million passenger cars were sold in 2010 compared to slightly more than a million in 2000; and in the case of excavators, domestic sales increased from 9,000 to 215,000 over the same period. Twenty years ago, these markets were often highly segmented between the products of domestic firms and multinationals—domestic firms serving the low end and multinationals serving the higher end through either imports or production in China. But increasingly we observe intense competition emerging between these two[43].

To be successful, investments in upgrading of local capabilities by both types of firms are required. For domestic firms, upgrading to improve product quality and variety, and thereby avoid the intense competition at the lower end of the market, has become essential; for foreign firms, it is investments in local sourcing, as well as development of local research and development (R&D) capabilities to help them modify their products in ways that make them more appealing to local customers. One major foreign automobile original equipment manufacturer (OEM), for example, developed a five-year plan in the mid-2000s to lower their production costs in China by 45 percent through exactly such measures.

In the Chinese context, especially important are the interactions and spill-overs between these two types of firms, which expand the pool of upgrading opportunities for OEMs and suppliers. Increasingly, Chinese firms are able to leverage the benefits from participating in multiple value-chains, for example, supplying local Chinese firms, more-demanding local foreign firms producing in China and then for the export market. Associated with each of these channels are different kinds of know-how and capabilities. Moreover, through mobility in the labour market, knowledge and experience acquired in foreign firms is being more broadly disseminated in the economy. This is pervasive.

Despite its depth, this process is highly uneven across sectors, with a host of restrictions and constraints continuing to impede the upgrading process and the reallocation of resources (skilled labour, capital, energy and raw materials) to the most productive of firms. Some estimate that total factor productivity (TFP) in industry could be raised by as much as twenty five percent if misallocation *within* sectors could be lowered to levels observed in the United States. There may be even larger gains to *inter-sector* reallocation, which are excluded in these calculations. In a country like the US, this reallocation represents an important source of productivity growth, but in China its role has been minimal.

These distortions are likely tied to continued imperfections in capital markets, regulatory restrictions on entry that preserve existing market power, difficulty of firm exit, policy preferences in key sectors for state-owned or state-linked firms, as well as continued subsidies to exporting. The state has retreated from many sectors, but in those in which it has remained, it often dominates. At a higher ("two-digit" industrial classification) level, for example, the sectors in which state firms have the highest revenue from output represent nearly two-thirds of total state output in industry. Moreover, the average state share in these sectors is 60.1 percent, compared to an average of 24.4. These sectors include power generation, transportation equipment, iron and steel, petroleum and coal mining.

Much more work needs to be done to identify these factors, but a number of things point to the likelihood that these impediments are largely policy-related and tied up in China's political economy, especially their non-economic objectives, at both the local and central level. In some circles in China, there are growing concerns of a return to highly *dirigiste* economic policies[44]. In all likelihood, the costs for the economy are very high.

There are also dynamic implications, as perceived constraints on firm growth may be impeding investment incentives of the most dynamic of firms in R&D, worker training, capital equipment, etc. because of lower expected returns. For example, concerned that SOEs are favoured in the market, non-state actors will not be willing to make as big investments because of lower future returns.

Automobiles, the heavy construction equipment sector and telecommunications provide a valuable contrast in the ability of domestic firms to emerge in the context of highly competitive domestic markets[45]. In heavy construction, a mix of private and state-linked firms such as Sany, Zoomlion, Longgong, Liugong and Xiagong have emerged over the course of the last two decades and are successfully competing with multinationals such as Volvo, Caterpillar and Komatsu in a growing array of products and product-market segments in both China and now in other emerging markets.[46] Amongst Chinese firms, we also see a growing market consolidation that is bottom-up as opposed to top-down. Telecommunication equipment, on the other hand, has parallels with heavy construction equipment, with local equipment manufacturers such as Huawei and ZTE early on successfully leveraging market opportunities in lower-tier cities in their upgrading efforts.[47]

Contrast this experience with the automobile sector, where Chinese firms continue to experience difficulty in competing domestically, let alone globally, and once again high on the agenda of policy-makers in Beijing is a top-down, administrative-led consolidation of market players that is simultaneously encouraging overseas acquisitions. In mobile handsets, government policy through the early 2000s handicapped the development of local firms through restrictions on licensing, and only innovations of MTK (Taiwan) and Google—through Android—significantly opened the door. Underlying these differences between sectors are several decades of state policies relating to freedom of entry, foreign direct investment, forms of technology transfer, tariffs, bankruptcy, as well as mergers and acquisitions that influence the incentives and channels of upgrading, and the ability of highly competitive indigenous firms to emerge.

Some of the same factors at work in industry help to explain even weaker performance in services which now constitute upwards of 45 percent of GDP. Earlier estimates suggest that productivity growth in services may be only fifteen to twenty percent of that in manufacturing. Services contribute directly to GDP, but are also an important input into manufacturing. The most recent national input-output table for China shows that the contribution of services (direct and indirect through their contribution to other intermediate goods) to manufacturing is 40 percent. In general, the reform and restructuring of services (for example, transportation, telecommunications, retail and wholesale trade, and financial services) lag reforms in manufacturing by a wide margin. Largely non-tradable, high prices in these sectors can be linked directly to low productivity. Industry and manufacturing are important, but China's ability to remain competitive and sustain robust growth will depend as much, if not more, on productivity performance in services, and here the record has not been promising.

Industry and manufacturing are important, but China's ability to remain competitive and sustain robust growth will depend as much, if not more, on productivity performance in services, and here the record has not been promising.

The Implications of China's Resource Quest

China's demand for minerals, oil, gas and agricultural products drives commodity production throughout the world and brings much needed capital to resource-rich countries. At the same time, the scale and scope of Chinese investment are shaping global commodities markets, governance practises and international security in new ways. In some cases, China's impact is nascent; in others, it is already profound. Most importantly, China's resource quest is an evolving process that is influenced not only by internal Chinese dynamics but also by the interaction of China with the rest of the international community.

China's resource demand and the market

Over the past decade, China has become the world's largest or second largest consumer of a wide range of primary commodities. The size of its population, its economic growth rate and its position as the second largest economy in the world all contribute to make it a significant force in global commodities markets. Its consumption of key commodities in 2011 gives some indication of its importance:

- China consumed 48% of global zinc supplies, 50% of lead, 50% of copper and 45% of aluminum. (In comparison, the United States consumed 8% of global zinc supplies, 15% of lead, 8% of copper and 6% of aluminum.) Mineral imports alone made up 30% of China's foreign trade;

- In agricultural products, China consumed half of all pork, almost one-third of global rice supplies, as well as one-quarter of the world's soybeans;

- China is the world's second largest consumer and importer of oil after the United States. In 2011, growth in China's oil consumption accounted for half of the growth in global oil consumption.

During 2006-2011, as China became the dominant importer of many base metals and agricultural commodities, its impact on global commodity prices increased steadily.[48] Some commodities are more sensitive to Chinese demand, such as soybeans, copper, oil and platinum[49], and as a result of growing Chinese demand, prices of iron ore rose almost tenfold between 2001 and 2011.[50] Other resources, such as natural gas, are not as susceptible to Chinese demand.[51]

China's preference is to import resources from Chinese-owned assets or joint ventures. A series of government white papers published during the period from 2000 to 2009 on grain, mineral and energy security makes clear that even as Beijing's confidence in the global market has increased, the Chinese leadership continues to believe that resource security depends on control over assets. According to one Chinese official, by 2015, China has called for 50% of its iron ore to come from Chinese-owned mines outside China.[52]

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Will Chinese demand continue to grow? The picture is mixed. Major domestic drivers of increased Chinese demand include urbanisation, rising income levels and shifting diets, none of which shows any sign of abating. Notably, China's commodity intensity is quite high: at the same level of economic development, China consumes about 35% more energy than Korea and twice as much as Brazil; and the difference in commodity intensity is even greater for base metals.[53] If China makes substantial improvements in its industrial efficiency, however, commodity demand could ease. Similarly, shifting the Chinese economy away from a capital intensive, export-driven economy to a services and consumption-based economy would contribute to a slowing of demand growth or even a levelling off.

Resources and governance

China's overseas investment in extractive industries is also shaping the economic and political landscape of many countries. China is now the largest provider of loans to the developing world, and the economic benefits of Chinese investment are easily visible in thriving mining industries, new highways, and active ports around the globe.

Chinese investment is also marked by a willingness to set aside political considerations. As Sahr Johnny, a former Sierra Leone ambassador to Beijing, noted in 2005, "We like Chinese investment because we have one meeting, we discuss what they want to do, and then they just do it... There are no benchmarks or preconditions..." Unlike the International Monetary Fund or some other countries, China does not qualify its loans with requirements for budget transparency or transparency in the distribution of resource revenues.

While the benefits of Chinese overseas investment are evident, the challenges have also become apparent. Corporate governance, environment, labour and safety violations, as well as a lack of socially inclusive growth have become hallmarks of Chinese investment.

Latin American officials and analysts, for example, have expressed apprehension over the large number of state-owned enterprises (SOEs) involved in China's overseas foreign direct investment. (During 2000-2011, 87% of China's overseas foreign direct investment in Latin America was from state-owned enterprises, and 99% of that was in companies involving access to raw materials and energy.[54]) They are particularly concerned over intellectual property rights and cultural preservation, as well as the potential for a political conflict with Beijing to bleed into the resource investment and vice versa.

Some countries, such as Canada, are taking steps to limit the influence of investment by foreign state-owned enterprises. In the wake of the buy-out of the Canadian energy firm Nexen by the Chinese National Overseas Oil Corporation (CNOOC), for example, Canadian officials announced new strictures on investment by SOEs, such as requiring them to demonstrate that they are free of political influence. Similarly, Chinese companies' efforts to purchase large tracts of agricultural land in Brazil led the Brazilian government to rewrite its land laws to limit the size and number of such purchases by any one firm.

Chinese resource investment has also been accompanied by complaints over damaging environmental practises. Chinese mining companies such as Peru's Shougang Hierro mine and the China Metallurgical Group's Ramu Nickel mine in Papua New Guinea have engendered widespread, ongoing environmental protests. In Argentina, Chinese agricultural firms have created concerns over land management and environmental practises. Nobel Prize laureate and president of the Foundation for the Defence of the Environment Raul Montenegro has spoken out explicitly about the challenge posed by China. "On a global level, China is the country most affected by the extension, intensity and economic impact of land degradation. So it is difficult to believe that they won't make the same mistakes with their land in Rio Negro as they have in their own country."[55]

The most politically sensitive issue with regard to Chinese investment revolves around labour and the widespread, government-supported practise of exporting Chinese labour to the target country. Chinese investment in a particular resource is often structured as a loan-for-oil, loan-for-gas or loan-for-minerals deal, in which the loan is either paid back or guaranteed in the supply of the commodity to China. In many cases, these loans also include a broad package of infrastructure projects, a number of which are required to be undertaken by Chinese contractors. In the case of a 2011 China Development Bank loan to Ghana, for example, the loan required that Chinese contractors implement projects worth 60% of the loan amount.[56] In Angola, where only 30% of the work financed by Chinese money must go to domestic firms, there are as many as 300,000 Chinese workers. Chinese managers often argue that Chinese workers are willing to work longer hours for lower wages. Even if the wages are not a consideration, the language barrier often is. Unsurprisingly, this has bred resentment and large-scale protests in many countries, including Zambia, Papua New Guinea, Vietnam and Zimbabwe, amongst others.

Some countries have responded by adopting new labour regulations that attempt to limit the potential influx of Chinese workers. In Mongolia, for example, immigrants from any one country are capped at less than 10,000 people, and foreign workers are limited as well. As a former vice finance minister stated, "We cannot afford to have one particular nation control our business."[57] In 2012, Vietnam passed a new law requiring that all foreign business give priority to Vietnamese workers; local government committees will be allowed to solicit Vietnamese workers before any foreign labour can be imported. At one construction site, for example, there were 100 Vietnamese workers and 760 Chinese.[58]

Beijing is increasingly sensitive to international claims that its enterprises are not operating up to international standards. In 2011, the Ministry of Commerce's Department of Outward Investment and Economic Cooperation noted that in Peru, companies specifically needed to "respect Peruvian law; consider environmental protection and keep good relations with workers to keep disagreements from spiralling out of control." Several large SOEs are also now participants in the UN Global Compact (an initiative that supports corporate best practises in human rights, environment, labour and anti-corruption), including China Minmetals, Chinalco and Sinosteel. There is also evidence of learning. While the Shougang Hierro mine has been widely reviled in Peru for its poor labour and environmental practises, Chinalco has earned points for its handling of the relocation of a local town, hiring of a Canadian firm to develop an Environmental Information Management system, and the fact that it did not bring in Chinese labourers.

Security implications

China's reliance on overseas resources is also contributing to a transformation of Beijing's broader security interests, particularly with regard to maritime security. Forty percent of China's oil, for example, relies on maritime transport.[59] Chinese analysts have identified three threats in this regard: pirates and non-state actors;[60] the potential of other countries, in particular the United States, to enforce a blockade of the Strait of Malacca; and sovereignty disputes with their neighbours in the East and South China seas.

Beijing has taken a number of steps to try to ensure the security of international transport routes and to protect its citizens working abroad. Some are defensive in nature, for example, developing overland supply routes, such as a pipeline through Burma to transport oil and gas from the Middle East and Africa to avoid the Malacca Strait. Over the past several years, the People Liberation Army's (PLA) Navy also has undertaken anti-piracy activities in the Gulf of Aden; it has participated in joint anti-piracy activities with a number of countries. Others, however, contribute to a greater offensive capability, such as arming fishing boats in the East and South China seas, formally adopting a doctrine that moves from a "near seas" to a "far coastal" defence and a ratcheting up of both PRC military rhetoric as well as naval capabilities. Still, other measures remain speculative, such as the potential establishment of military bases, where China has been developing or modernising ports in areas such as Pakistan, Bangladesh and Sri Lanka. China has already established a naval "supply and recuperation" facility in the Seychelles, although it insists that it will not station abroad. (Some analysts, such as Fudan University's Shen Dingli, have nonetheless suggested that China should not take military bases off the table. As Shen argued in 2010, "It is our right. Bases established by other countries appear to be used to protect their overseas rights and interests.")

Conclusion

China's growing demand and outwards quest for resources to fuel its continued economic growth have raised the spectre of rising commodity prices and shortages, deteriorating governance conditions in resource-rich countries, and a growing, potentially assertive Chinese military presence globally. While such concerns are not unfounded, they also are not preordained. China's development trajectory and political choices at home will influence significantly the structure of its future resource demand.

Resistance to Chinese state-owned investment on environmental, labour and corporate governance grounds is already producing a shift in the practises of some Chinese companies. A broad-based push by the international community to engage China more deeply on joint anti-piracy exercises as well as on naval coordination could help ensure greater stability rather than uncertainty in maritime security. While China's resource security needs and strategy are overwhelmingly domestically driven, the international community nonetheless can play an important role in determining how China's policies and influence evolve.

China's Acquisition of Natural Resources Abroad: Australia's Experience

Ever since the development of iron ore and coal exports to Japan in the 1960s, followed by the development of similar relationships with South Korea and Taiwan, trade and investment in resources have played a crucial role in Australia's security in the broadest sense, including economically and socially. Through growing levels of prosperity, it has also strengthened the country's abilities and credentials as a security partner in a narrower, strategic sense. However, its increasing trade and investment links with China have far outstripped any of these earlier relationships in both speed and scale, and Canberra is still feeling its way as to the longer-term impact of this.

China is now Australia's top trading partner, accounting for over 22% of total trade. Two-way trade today stands at around A$100 billion while it broke the A$10-billion mark in 2002. The current figure is over 80 times that of 1982. Further, since 2001 the balance has been clearly in Australia's favour.

In 2010 resource exports made up 57% of Australia's total export receipts. Almost 70% of iron ore and 18% of coal exports went to China. In the same year, 37% of Australia's total resource exports went to China.

Looking at the terms of trade, they are currently 65% higher than the average for the 20th century, and 90% higher than the average for the 1990s. China is in large part responsible for this—as it is for the fact that of all OECD countries, Australia was one of the few that did not go into recession during the global financial crisis of 2007-09.

In 2008-2009, China was the second largest investor, with investments totalling A$26.6 billion. In 2009-2010, it ranked third largest with A$16.3 billion. Around 80% of this investment is in mineral exploration and resources processing. It should be pointed out, however, that despite the dramatic growth of Chinese investment in Australia, in terms of total foreign direct investment (FDI) into Australia Beijing lags far behind the UK, the US and Japan, for many years the largest overseas investors down under.

Precisely because of the speed and scale of these unprecedented developments, Australia is now on a very sharp learning curve, and this applies equally to popular opinion, media, business, academia and a range of government processes, analysts and decision-makers.

This was highlighted dramatically by the almost perfect storm in Australia-China relations between 2008 and 2009. It began with the events in Lhasa in 2008 and the way this played into the progression of the Olympic Torch around the world. In Australia, there were no seriously untoward incidents, but on the day of the torch's run through Canberra we saw the nation's capital turned into a sea of red flags waved by patriotic Chinese students from across the country, assisted by the Chinese embassy and consulates. The impact on the citizens of Canberra, and across the country, was significant. Then came a series of controversies: the mining company Chinalco's attempted bid for a larger stake in an Australian competitor, Rio Tinto; the crude and badly handled Chinese interference in the 2009 Melbourne Film Festival over a film about Uyghur exile leader Rebiya Kadeer, and her subsequent visit to Australia; the arrest of Rio Tinto's representative in Shanghai, Stern Hu, seen by some as retaliation for the rejection of Chinalco's bid (by British shareholders, not the Australian government, as some in China believed to be the case); and the ambiguous messages regarding China in Australia's 2009 Defence White Paper, which went down badly in Beijing, prompting defensive responses in Australia. The Chinese were also disappointed in Kevin Rudd's failure to be a "friend of China", as they would have preferred it, rather than in his chosen capacity as a "*zhengyou*" (one who demonstrates his friendship through frank criticism when it is called for).

This was the strained bilateral environment in which vigorous if not always well-informed debate about Chinese investment, most particularly investment in natural resources (later expanded to include the equally if not even more visceral issue of agricultural land) unfolded. To the typical concerns about foreigners investing in these areas was added the fact that, in China's case, many of the real or potential investors were from state-owned enterprises (SOEs). Through this period the image of China, which had been generally quite positive in Australia, was also beginning to change for the worse. It was not only SOEs *per se* that presented a problem, but also the nature of the state that owned them. More generalised concerns about a rising China as a Party-state beginning to challenge the US-dominated Asian-Pacific order also influenced reactions to Chinese investment and the question of the longer-term implications of Australian dependence on the resource trade with China.

In a 2011 poll conducted by the Lowy Institute for International Policy, some 75% of Australians agreed that China's growth had been good for Australia, up 8 percentage points since the question was first asked in 2008. However, the Lowy also runs a chart tracking the feelings Australians have towards a number of major countries which trend negatively for China. In 2006, China and the United States were on the same level. Six years later, a gap of 19 percentage points had developed, with a simultaneous rise in US popularity and fall in that of China—to the same level as Indonesia, traditionally regarded with suspicion, at least at the popular level. According to the Lowy, in 2011 57% of Australians polled said the Australian government was allowing too much investment from China, the same figure as for 2010, up 7% from 2009. Also, 35% said the amount was right, and only 3% said more was needed.

Most significantly, despite the extraordinary rise of China's economic importance to Australia, fully acknowledged by those polled, around 44% felt that China would become a military threat to Australia in the next twenty years.

For the Australian government, in terms of managing investments, as well as handling public perceptions and domestic politics, a crucial element concerned the operation of the Foreign Investment Review Board (FIRB). The FIRB was originally established in 1976 in response to public concerns over growing investment from Japan (and from the United States). It was tasked with reviewing larger foreign investment proposals using the test of "national interest" in order to maintain community confidence and de-politicise the approvals process. Since its establishment, the government has officially rejected only two proposals, although several have been withdrawn as a result of what the initiators considered unacceptable amendments being required prior to approval.

The application of the national-interest test, however, has not been without its critics, not least for its opacity. While the original intention in creating the FIRB was to reduce the political pressure on decision-making regarding FDI proposals, heightened levels of concern over Chinese investment in the context of the bilateral troubles of 2008-2009 were directly reflected in additional, and arguably unnecessary, considerations and amendments being included in the review process following FIRB reviews in 2008. Significantly, this period also saw a breakdown in the bi-partisan approach to foreign investment issues, with the opposition taking a more populist stance. This stood in contrast to that enunciated by former coalition Prime Minister John Howard, who said: "You've got to remember that when a company invests, whether it's state-owned, partly state-controlled or not, it still has to comply with the laws of Australia and it's quite possible for the treasurer of the day to impose conditions on investment". This statement touches on two crucial issues: the question of state ownership, and the overall regulatory framework and the ability of the government to ensure its proper functioning.

The prevalence of SOEs in Chinese investments in Australia has raised concerns that the Chinese authorities may use these investments as a vehicle for pursuing geopolitical strategies. It is feared that, because every SOE includes a Party committee in its midst which is ultimately responsible to the Party centre, Beijing could exert pressure if it decided to punish Australia or use its economic clout to pursue its goals. It is not unreasonable to make this assumption in considering the security implications of Chinese SOE investments and a good deal of work has been done to test this assumption. However, most scholars and officials who have worked in this area are struck by the degree to which SOEs abroad tend to behave more like commercial entities, including in quite competitive fashion, than as obedient followers of Chinese government strategies. Domestically, too, corporate governance of Chinese SOEs is evolving towards a system increasingly driven by market disciplines, and reform is likely to intensify as their international interests are subjected to more scrutiny by Chinese authorities as well as host-country regulatory processes. It seems the most we can say about the worst-case scenario is that, while it is theoretically possible, the evidence is not yet available. This does not mean we should not be continually alert to any signs of such behaviour, but neither should we allow such concerns to lead us to act in ways which damage our own economic security interests.

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There is a separate issue concerning the quality of SOE businesses. Many have been characterised by less than optimal efficiency, with “fat and lazy” managerial and work practises encouraged by their links to government, subsidies, etc. Over time, too great a presence could lead to an overall pollution of the business environment in the host country. Some are simply inexperienced and do not understand the local business environment. However, here too, as with the previous consideration, local regulation and oversight form the first line of defence.

An additional consideration is the danger of China using its SOEs to behave in a mercantilist fashion for strictly political purposes, as we saw in the case of rare earths and Japan. That is for two reasons. First, China’s action was extremely short-sighted and in the longer term more damaging for China’s interests than those of Japan. Second, where the resource relationship with Australia is concerned, the scale and nature of our trade and investment links do not readily lend themselves to such actions. China has just as much reason to worry about dependency as we do, and indeed it does. Over the past decade China's foreign dependence for key minerals has risen sharply. In 2010, its dependency ratios were 43.8% for copper, 62.1% for iron ore and 78.0% for aluminum. This is of course the main reason why China's investment policies have explicitly identified natural resource acquisition as a central strategic objective of internationalisation.

The other side of this coin is the concern that Australia could become overly dependent on the resource trade and investment relationship with China, and hence become vulnerable to changes in demand. While the country enjoys a favourable geography, impressive natural wealth and political stability, it is not the only game in town. Some authoritative analysts worry that lack of clarity around the FIRB's processes, perceptions in China of increased investment risk, as well as costly and embarrassing public failures could accelerate the relocation of Chinese investment to other countries. China can go to Africa, just as Japan went to Brazil to fill the Australian gap thirty years ago.

The case the Chinese most often raise when complaining about Australian policies is the attitude to Huawei's proposed involvement in national infrastructure. The irony here is that the issue has nothing to do with the FIRB on investment policies, but reflects a judgement made on security grounds by the relevant authorities. While this relates to assumed links between Huawei and certain Chinese agencies, Huawei is not an SOE but a private company. Whatever the details of the case, this should demonstrate quite clearly that, when there are perceived security risks, there are both capable agencies and the necessary legislative framework to handle such issues as they come.

The final point is that ultimately all these concerns relate to the big issue of the rise of China and what that portends for Australia's national security in the very broadest sense. However, given that the country's economic well-being depends to a significant degree on continued Chinese growth, Canberra is unlikely to decrease *deliberately* economic exchanges in case a wealthier and more powerful China may *eventually* act in ways contrary to its interests. Of course it may—and it may do so regardless of the state of our economic ties. Then again it may not, or those ties may themselves help ameliorate future Chinese attitudes. There is a need to place legitimate and rational security concerns in the context of our crucial economic interests.

China and the Arctic

The Arctic's potential in the 21st century

Rising temperature in the Arctic is causing a retreat of sea ice and a lengthening of the summer season. These unprecedented changes have prompted a reassessment of the region's economic potential and given rise to new political issues. Projections of the date when the Arctic Ocean will first be free of sea ice during the summer season have moved forward in recent years, from the end of the 21st century in a 2007 report by the International Panel on Climate Change (IPCC) to within the next 25 to 40 years in more recent studies. The warming of the Arctic is making possible circumpolar navigation that makes possible the redrawing of transportation routes, the emergence of new port cities and reduced transport time between Europe, Asia, and North America – in some cases by more than two weeks. The warming of the Arctic could also extend exploration and drilling seasons for offshore oil and gas, and mining for minerals. The Arctic is appraised to hold vast natural resource potential. The US Geological Survey estimated that the Arctic contains 30% of the world's natural gas and 13% of the world's oil reserves. It is also rich in minerals such as coal, nickel, copper, tungsten, lead, zinc, gold, silver, diamonds, manganese, chromium and titanium.

Drivers behind China's interest in the Arctic

According to Russell Hsiao of the Project 2049 Institute, as a fast growing economy, China is supplementing its domestic supplies of energy with imported fuel resources. Furthermore, while China has abundant domestic coal, it is slowly weaning itself off of coal as the main source of power generation and importing oil and gas.

If they became accessible, gas and oil supplies from the Arctic, using an Arctic route, would be more secure than supplies from the Middle East and Africa, where both piracy and unstable governments are of great concern. Chinese scholars have noted that an Arctic route would circumvent the coast of developed nations, where stability is common and piracy is not. A viable Arctic route could also alleviate China's "Malacca Dilemma". It is estimated that about 60% of international vessels passing through the Strait of Malacca are either Chinese-flagged ships or container ships transporting cargo for China. China is feeling insecure about its heavy reliance on this strategic waterway, which it does not control.

Given the commercial and security implications, China wants to be regarded as a legitimate player in the Arctic. Knowing full well that it is not geographically located in the Arctic, China has started to refer to itself as a "near Arctic state" and an "Arctic stakeholder". Becoming a permanent observer to the Arctic Council is another avenue to gain legitimacy as an Arctic player. Furthermore, as a permanent observer, it will gain fuller access to related debates, such as the accessibility and governance of the various Arctic transportation routes.

There is also a degree of political bravado involved. As a permanent member of the Security Council, China likely believes it should be involved in all global affairs.

Chinese activities in the Arctic

Expeditions and navigation

In the summer of 2012, China's sole icebreaker, *Xuelong*, or Snow Dragon, completed its fifth Arctic expedition. More impressive, *Xuelong* sailed to the Arctic using the Northern Sea Route, but returned from the Arctic using the Polar Route, bypassing both the Northern Sea Route and the Northwest Passage. This is particularly significant since the Polar Route lies in international waters and is the shortest route.

China is also increasing its investment in Arctic seafaring hardware. Chinese policy-makers recently decided that *Xuelong* needed "brothers and sisters". Moreover, instead of purchasing icebreakers from another country, China has decided to build the second icebreaker in its own shipyard, although using Finnish and British technical know-how.

Presence in the scientific community

University research departments and government-affiliated research institutes have been created in cities such as Beijing, Dalian and Shanghai for dedicated academic and scientific thinking on the Arctic. In 2004, China gained a physical scientific presence there by establishing the *Huanghe*, or Yellow River, research station in Norway. However, despite the infrastructure being set up specifically for research, it is worth noting that China does not have a dedicated budget line for Arctic research.

Diplomacy efforts

Even though Nordic countries were the first western nations to recognise the People's Republic of China after its establishment in 1949 (Sweden, Denmark, Norway and Finland in 1950; Canada in 1970; Iceland in 1971), no senior-level visits from China to the Nordic countries occurred until recently. This marked increase in diplomatic activity at the highest levels of China's government is evidence of China's growing interest in the Arctic.

From 2005 to 2010, Norway had the most active relationship with China of the Nordic countries. Norway saw a flurry of visits by vice-premiers (2005, 2006), vice foreign ministers (2006, 2007, 2010), the minister and vice minister of commerce (2006, 2010), as well as senior officers from the People's Liberation Army (PLA), such as Chief of General Staff General Chen Bingde (2008) and Chief of PLA Navy Admiral Wu Shengli (2009). Norway and China also established a bilateral dialogue on Arctic affairs.

Senior officials have made inaugural visits to almost all of the Nordic countries in recent years, despite the freeze in relations with Norway in 2010. Chinese president Hu Jintao visited Sweden in June 2007 and Denmark in June 2012. In March 2010, Vice President Xi Jinping visited Sweden and Finland. In April 2012, Premier Wen Jiaobao visited Sweden and Iceland.

Economic engagement

With high-level political contact came economic engagement. Indeed when Premier Wen Jiabao visited Sweden in April 2012, five bilateral trade deals were signed with the government, and six agreements were signed with companies. During his June visit to Iceland in the same year, Wen Jiabao also signed a number of economic agreements, covering areas like free trade and continued geothermal energy cooperation. Denmark received a trade delegation ahead of any visit from a Chinese head of state; in May 2010, Chinese Minister of Commerce Chen Deming led a trade and investment promotion mission that included more than 100 Chinese entrepreneurs. This was the largest Chinese trade delegation to visit Denmark.

Greenland's minister for industry and mineral resources was greeted by Vice Premier Li Keqiang in China in November 2012. A few months later, China's minister of land and resources, Xu Shaoshi, travelled to Greenland to sign cooperation agreements.

Greenland has substantial deposits of minerals, including rare earths, uranium, iron ore, lead, zinc, petroleum and gemstones. However, Greenland has presently only one working mine. More than 100 new sites are being mapped out by prospecting companies of various nationalities. For China, large Chinese companies are financing the development of mines identified by these smaller prospecting companies. For instance, London Mining, a British company, is in talks with a state-owned Chinese steel-maker to finance and build a US$2.3 billion iron mining operation 175 kilometres north of the capital, Nuuk. China plans to import 2300 Chinese workers (against Greenland's population of 57,000). A vast majority of the iron extracted in the mines would be shipped back to China.

According to *The New York Times*, China also proposed building runways for jumbo jets on the ice in Greenland's far north to fly out minerals until the ice has melted enough for shipping. Chinese mining proposals often include infrastructure building. In Canada, Chinese firms have acquired interests in two oil companies that could give them access to Arctic drilling. In addition, the Canadian government is currently considering a multi-billion dollar mining proposal in the Izok Corridor in western Nanuvut. The project would consist of two mine sites, an all-season access road and a port facility. The mines are expected to produce 180,000 tonnes of zinc and 50,000 tonnes of copper a year. To transport and ship these mineral concentrates, the all-season access road would extend north to connect the two mines (Izok and the High Lake) and end further north at a proposed port at Grays Bay on the Coronation Gulf. The planned port would accommodate ships of up to 50,000 tonnes and which could make 16 round trips a year—both east and west—through the Northwest Passage.

Chinese debate on the Arctic

According to Linda Jacobson of the Lowy Institute for International Policy, in the Chinese system, the formulation of an official policy position is usually preceded by a period of open debate. We are witnessing that right now. Although the initial focus of China's Arctic research was on climate change and its environmental consequences, there has been a steady flow of assessments on the commercial, political and security implications for China of a seasonally ice-free Arctic.

Li Zhenfu of Dalian Maritime University has stated that, "whoever has control over the Arctic route will control the new passage of world economics and international strategies". Another prominent scholar of the region, Guo Peiqing, of the Ocean University of China, opined that it is not in China's interest to remain neutral in Arctic politics and added that "any country that lacks comprehensive research on Polar politics will be excluded from being a decisive power in the management of the Arctic and therefore be forced into a passive position".

Perhaps the most alarming assessment came from the military. In a rare open-source article by a military officer titled "The Closely Watched Dispute Over Arctic Sovereignty," PLA Senior Colonel Han Xudong noted that due to complex sovereignty disputes in the Arctic, the possibility of using force cannot be ruled out.

China might not yet have a fully-formed, clearly articulated Arctic strategy, but it certainly is clear about its objective: to influence Arctic affairs and have a role in its governance structure. It is doing so by impressing upon its audience that Arctic affairs are international, not regional issues. In an official speech given by Hu Zhengyue, the assistant minister of foreign affairs, in 2009, Hu urged the Arctic states to recognise the interests of non-Arctic sates, and also to consider "the international submarine area" as belonging to "the common human heritage" and that they should "ensure a balance of coastal countries' interests and the common interest of the international community."

Yet recently, China's public narrative on the Arctic is becoming more subdued. It is recognizing that overly proactive statements on resource and sovereignty issues are alarming Arctic states and consequently, undermining the position it has gained. It has dropped the words "evaluation of polar resource potential" in the Five-Year Plan's polar project. Also, an increasing number of researchers are recommending that climate change be prioritised in China's Arctic agenda. However, it is important to note that these adjustments are made to circumvent the sensitivity of discussing Arctic resource and sovereignty issues; they do not mean the expulsion of these issues from Chinese thought.

Arctic states' reaction to China

Arctic states are justifiably interested in Chinese activities in the Arctic. The Arctic has for a very long time been their exclusive backyard and now a number of countries with no direct territorial claims in the region are also expressing interest in this arena. China is unique amongst the newcomers in terms of its political and economic heft as a "rising power".

The Nordic reaction to China is mixed. While Iceland initially welcomed China's investments, there has been some trepidation, as evidenced by the government's rejection of Huang Nubo's US$200 million proposal to purchase or lease 300 square kilometres of land for eco-tourism. However, the country's recent proposal for the creation of an Arctic Circle, which will be open to China and other non-Arctic state, presents an opening of which Beijing is certain to take advantage. Norway was also one of the first to welcome China into the Arctic, but its view of China has dimmed since relations were unceremoniously put on deep freeze after the Nobel Peace Prize award to Liu Xiaobo. Greenland, on the other hand, has insisted that it will not treat China any differently than the EU, despite the latter's request for a preferential investment climate. Scholars have surmised that Greenland's position has the tacit support of Denmark, an EU member.

Canada shares many of the Nordic countries' concerns but also understands the economic opportunity that Chinese capital could offer. A key question is how to balance economic opportunity with potential security risks. Some also wonder about the possibility of China becoming a political ally: given its position in maritime sovereignty disputes elsewhere in the world (notably in the South China Sea), perhaps it would be sympathetic to Canada's sovereign claims in the Arctic, including the Northwest Passage.

The US understand China's interests in Greenland's natural resources, its decision to build, instead of purchasing, a new icebreaker, as well as its focus on the strategic impact of new transportation routes for commercial and military purposes. Nonetheless, Washington takes a holistic view of the Arctic and its mission to maintain freedom of the seas. Both NORTHCOM and the US Navy have noted that a sound US polar strategy includes enhanced communications, domain awareness, infrastructure and presence.

Russia has a fairly matter-of-fact response to China. An official at Russia's Ministry of Foreign Affairs summarises the Russian position: "Understandably, China is concerned about the Arctic due to its rich resources, but the country does not have the right to make any decision regarding the region". At the same time, "it is correct for the Arctic nations, including Russia, to cooperate with non-Arctic nations". Russia also readily acknowledges that since China will increase its interest in navigable routes and resources in the Arctic, the region could be a fruitful area for cooperation—and presents high potential area for discord—between the two countries.

Potential partnerships between the Arctic states and China

Chinese officials understand that their country needs to partner with foreign companies to extract energy and minerals in the region; most Arctic oil and gas is found on the near-shore continental shelves of the Arctic states. In general, the Russian Arctic is considered to contain more gas and the offshore Norwegian and North American areas (ie. Alaska, Canada and Greenland) more oil. In addition, China lags behind western deep-sea oil and gas exploration and exploitation techniques and technologies. Taken all together, Arctic watchers wonder about the prospect of a partnership in which Russia supplies the drilling rights to natural gas, a Nordic nation supplies the deep drilling capability, and China supplies the capital to finance it all.

Political calculations, not political speculation

There are three main attractions fuelling China's interests in the Arctic: natural resources, trade routes and political prestige. All three require China to "play nice" with Arctic Council states, because China needs their support in order to operate—and operate with legitimacy—in the region. Most of the natural resources lie in exclusive economic zones (EEZs), and although China has the capital, it is the Arctic states that possess the knowledge and technology for deep-sea drilling.

China has made its own calculations about the value of becoming more attached to the Arctic Council. Being an observer in the Arctic Council is a means, not an end. China is seeking greater participation in the Arctic Council not because it wants to be part of an international regime and cooperation mechanism, but because enhanced membership would allow it greater access to Arctic politics, which would have a direct bearing on Chinese Arctic interests. If permanent observer status in and of itself was important to China, it would not have treated Norway so coldly after the 2010 Nobel Peace Prize was awarded to Liu Xiaobo ("for his long and non-violent struggle for fundamental human rights in China"). Norway is not just any Arctic state; it is one of two Arctic states to have held a formal bilateral dialogue on Arctic affairs with China (the other being Canada), and it is on Norwegian territory that China has its sole Arctic scientific research station.

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The Security Implications of China's Use of Cyberspace and Related Trends

Any discussion of China's cyberspace strategy typically begins with its domestic controls, and specifically the so-called Great Firewall of China (GFW). Secrecy surrounds the GFW but it is China's Internet backbone around cyberspace controls, the country's deepest layer of communications infrastructure through which all Internet traffic must eventually pass. Requests for content that contain banned keywords, domains or IP addresses are routinely blocked. Unlike other countries that impose national Internet censorship regimes and who present back to the user a "blocked" or "forbidden" page, the Chinese system sends a "reset" packet that disables the connection and sends back a standard error message giving the impression that the content requested doesn't exist ("file not found") or that something is wrong with the Internet. What other functionalities are contained in these gateway routers (eg, deep packet inspection) is unknown at this time; however, most analysts suspect that the gateways are designed not just to block content but to monitor network traffic and communications.

The GFW is part of an elaborate regime of domestic cyberspace controls, one element in China's overall information and communications strategy. It is reinforced by laws, policies, regulations in an effort to control the country's communications ecosystem. Contrary to principles of network neutrality, Internet service providers (ISPs), hosting companies, websites, chat clients and blogs operating in China are all required to police content flowing through their networks. Internet cafés are routinely surveilled. All individuals and organisations are held accountable by law for what they do and post online. According to a 2010 white paper published by the Chinese government:

> *No organisation or individual may produce, duplicate, announce or disseminate information having the following contents: being against the cardinal principles set forth in the Constitution; endangering state security, divulging state secrets, subverting state power and jeopardising national unification; damaging state honour and interests; instigating ethnic hatred or discrimination and jeopardising ethnic unity; jeopardising state religious policy, propagating heretical or superstitious ideas; spreading rumours, disrupting social order and stability; disseminating obscenity, pornography, gambling, violence, brutality and terror or abetting crime; humiliating or slandering others, trespassing on the lawful rights and interests of others; and other contents forbidden*

> *by laws and administrative regulations. These regulations are the legal basis for the protection of Internet information security within the territory of the People's Republic of China. All Chinese citizens, foreign citizens, legal persons and other organisations within the territory of China must obey these provisions.*

China routinely downloads responsibilities to police the Internet to the private sector, which must follow regulations in order to operate there. In 2008, the Citizen Lab, a multi-disciplinary laboratory of the University of Toronto, discovered that the Chinese version of Skype (TOM-Skype) was coded in such a way that it secretly intercepted private (and encrypted) chats whenever people used any number of banned keywords. Despite the outrage after the release of that report and Skype being condemned for colluding with China, four years later the same system is still in place. In fact, it is now more elaborately designed and frequently updated, sometimes on a daily basis, in response for example to current events like the ongoing dispute with Japan over islands in the South China Sea or the controversy around disgraced Communist Party official Bo Xilai. All Internet companies operating in China—Baidu, Sina, Tencent, Youku, QQ, etc.—are required to pledge self-management to stop the "spread of harmful information" over their networks. The policing is typically undertaken through filtering and surveillance of the type Skype engages in, enforcing the use of real names in registration processes (to eliminate anonymous postings), and even direct intervention by paid officials in forums warning users not to engage in unwelcome, perhaps illegal discourse.

While downloading controls to manufacturers of equipment and services is routine in China, occasionally there is resistance. For example, a proposal to have all new personal computers (PCs) manufactured in China come pre-equipped with the "Green Dam" censorship system was met with widespread condemnation from users and subsequently withdrawn. However, while the Green Dam represented a serious request, even for the Chinese government, more often than not companies simply comply in order to do business.

The system is hardly foolproof. Researchers at the University of Cambridge, for instance, once demonstrated how easy it would be to disable the GFW, and that even without outside meddling the gateway routers can be overwhelmed by peak usage. Technical means to circumvent the GFW are plentiful. Using tools like Tor, Psiphon and commercial virtual private networks (VPNs), many users play cat-and-mouse with authorities, with millions breaking through on a daily basis. Chinese citizens have also proven themselves adept at outflanking and mocking the censors. Code words, alternative metaphors, neologisms and ingenious images circulated as Internet memes are used in place of conventional terms to circumvent Skype and other company's filtering and surveillance regimes. In spite of these controls, there is a very dynamic Internet culture in China—and the Internet is often the source of considerable criticism of organised crime, corruption and government policies. But such criticism takes place in an environment that is tightly monitored and regulated, with an atmosphere of self-censorship reinforced by occasional high profile arrests of those who breach the system.

China's rapport with the information space

It is worth noting that China's cyberspace strategy is not aimed at completely isolating the country's population from outside influence. Rather, it is deliberately designed to take advantage of information and communications technologies, which the Chinese see as critical to their long-term future, while maintaining political stability around one-party rule. Continued economic prosperity is essential to the legitimacy of the Chinese Communist Party, and information and communications technologies are a central ingredient to a burgeoning knowledge economy.

Often ignored is the connection between China's domestic controls and the international dimensions of its cyberspace strategy. One of China's international objectives appears to be the exploitation of cyberspace for intellectual property, political espionage and targeted threats against human rights, as well as ethnic and religious groups the government describes as "separatists", "terrorists" or supported by "foreign hostile forces." It has pioneered ways to vacuum up information of strategic value to the government and national industries from the Internet directly, and done so seemingly without shame. The probe of Ghostnet[61], a global cyber-espionage ring, may have been one of the first to expose what this looks like from inside out, but it was neither singular nor unique, as evidenced by a report released in February 2013 by the US firm Mandiant[62]. Evidence of Ghostnet-like compromises now surface almost

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weekly and reveal a level of audacity and rapaciousness that is remarkable: dozens of government departments, from intelligence services to politicians' offices in numerous countries have been penetrated, with the perpetrators having operated out of China-based Internet networks.

The Nortel case is particularly noteworthy. In 2012, ex-Nortel employee Brian Shields, who had led the forensic investigation of the compromise, came forward to disclose his experiences. According to Shields, the breach was so thorough that the attackers, which Shields traced back to IP addresses in China, had control of seven passwords from the top company executives, including the CEO, giving them direct access to the company's internal secrets and intellectual property. (Attackers downloaded technical papers, research reports, business plans, employee emails and other documents from computers under their control.) Shields discovered the breach in 2004 but found his warnings constantly ignored by top executives. He estimates that the compromise had been going on since at least 2000 and lasted nine years. Nortel went bankrupt in 2009. Could there be a link between the Nortel breaches and the rising fortunes of Nortel's main China-based competitors, Huawei and ZTE?

In 2012, the China state-owned company, Sinopec, made a controversial bid to acquire Talisman Energy, one of Canada's top oil and gas exploration companies, for over $1.5 billion. While news reports focused on the question of foreign ownership of national assets, few noticed that Talisman Energy had become the victim of a major China-based, cyber-espionage operation called "Byzantine Hades" in 2011. The attackers gained access to Talisman's Asian-based networks, and had control of them for over six months. (Notably, a Bloomberg News report on this issue disclosed that the same Chinese attackers, known as the "Comment Group," had infiltrated the computer of a Canadian Immigration and Refugee Board adjudicator who was involved in the case of Lai Changxing, a Chinese tycoon ultimately extradited by Canada to China, where he is now serving a life-sentence in prison.) There is no evidence connecting the hack to the Talisman take-over bid, but it certainly raises some intriguing questions as to whether and to what extent information gleaned by the attackers made its way to state-owned Sinopec.

Also often overlooked are the civil society and non-governmental targets of cyber-espionage, whose victims are seen by China's leadership as being captured, or at least substantially supported, by "foreign hostile forces" rather than as expressions of legitimate domestic discontent. There appears to be little effort to address the root causes of this discontent; China's strategy is to infiltrate, disrupt and quash. Remarkably, the attacks against these groups are fairly indistinguishable from those targeted at foreign governments and private firms. Indeed, the same perpetrators often attack both. Both the Luckycat and Comment Group campaigns, for example, targeting energy, aerospace and other high-tech industries and government computers in several jurisdictions around the world, have impacts on civil society. Very rarely, though, do these groups' breaches attract the type of attention that other espionage cases receive. It is not profitable for cyber-security companies to focus their efforts on such groups. Those almost always lack the resources or capacity to handle the security problem themselves, relying often on small staff and poorly equipped infrastructure.

While cyber-theft and espionage are indeed threats, the potential military implications of China's cyber activities are more serious. It is unlikely that China would see any benefit in an armed conflict with the United States, but Chinese military literature emphasises the People Liberation Army's (PLA) capacity to destroy US satellites, as well as its other surveillance systems, should war break out. Like many other countries, China's military planners have fully integrated cyber-warfare into their military doctrine and operational plans. As the US has a military alliance with Taiwan and Japan, in the event of a regional war the People's Liberation Army would be hard pressed *not* to deploy its cyber-warfare assets to confuse, deter and even disable American military and civilian assets. When considered in light of the spill-over effect that might arise from their routine targeting of civil society, the potential for unintended escalation should be taken seriously.

Part of China's international strategy revolves around the setting of technical standards, like those relating to wifi protocols. In the early 2000s, China lobbied unsuccessfully to have its WAPI standard adopted internationally, losing out to the ISO approved 802.11 version. So the Chinese government turned to promoting WAPI as the domestic standard instead, making many handsets less than fully functional. For example, the official Chinese iPhone offered by China Unicom did not include wifi (which helps explains the burgeoning iPhone grey market in the country). However, in 2010 Apple introduced a new generation of its iPhone with the China-preferred WAPI wireless standard on its handsets, as did Motorola and Dell. It is noteworthy that Huawei is now the world's largest telecom-equipment manufacturer, bypassing Sweden's Ericsson in 2011, and China's Lenovo is now the second-largest PC maker in the world, behind only Hewlett-Packard. Technical standards are the *sine qua non* of cyberspace control: they shape the realm of the possible, structure the limits of what is permissible and define a path of dependency for future trajectories of technical development that is difficult to escape. Chinese investments in information and communication technology infrastructure around the world, as in Africa, should be viewed in light of the power and influence the standard will generate. Being built "from the ground up", Africa could be set on a path of "surveillance by design".

Future prospects

While technical standards-setting may work in indirect ways to further China's influence abroad, its policy engagement at regional and international forums is also important to note. China's participation at international forums where global cyberspace rules are debated has grown significantly, and its agenda is more clearly articulated and promoted. China's presence is increasingly felt, as it sends large, well prepared delegations to the Internet Corporation for Assigned Names and Numbers (ICANN), the Internet Engineering Task Force (IETF), the International Telecommunications Union (ITU), the UN Group of Governmental Experts on Cyber Security and the Internet Governance Forum.

Beijing is also active at a regional level, as evidenced by its leadership, along with Russia, in a regional security alliance called the Shanghai Cooperation Organisation (SCO). The SCO also includes Kazakhstan, Kyrgyzstan, Tajikistan and Uzbekistan. Afghanistan, India, Iran, Mongolia and Pakistan enjoy observer status, and Belarus, Sri Lanka and Turkey are "dialogue partners". The SCO is used to coordinate security concerns, primarily through the "Regional Anti-Terror Structure", known by its acronym, RATS. At RATS and SCO meetings, member states' security services coordinate anti-terror exercises and share information on "threats"—which many human rights groups suspect includes domestic opposition groups in an effort to restrict revolts.

It was once fashionable to think that China, like other authoritarian regimes, would wither in the face of the Internet and other new technologies. As powerful are these technologies can be, the Chinese government has shown that they can be made to serve anti-democratic ends, too. Given the increasingly strident messages sent by US officials to China regarding cyber-espionage, we may be entering a new, less predictable phase. The risks that unintended actions may lead to serious instability are indeed growing.

As we consider means to mitigate these risks and the bleeding of our industrial base from unabashed cyber espionage, we would do well to remind ourselves of a fact that may be easily overlooked. First, China's domestic problems in the human rights arena are a major factor driving its cyber insecurity abroad. China's aggressive targeting of foreign hostile forces in cyberspace includes groups simply exercising their basic human rights. We may well soften China's malfeasance around corporate and diplomatic espionage, but without dealing with the civil society dimension of the problem, at times neglected, we will not eradicate it entirely.

Confucius Institutes: Distinguishing the Political from the Cultural

The purpose of this article is to address the division of opinion amongst academics over the desirability of hosting Confucius Institutes (CI) on university campuses that has been growing since the first CI was established in Seoul in 2004. This will be done by first explaining the political mission of the CIs and their links with the Chinese Party-state. It will then be possible to draw on the evidence of various reports to assess the risks posed to the educational mission of universities. The article will finish with a plea to manage the problem of the CIs by clarifying the ethical principles universities claim to uphold, considering the implementation of governance mechanisms to ensure these are widely known and applied in a transparent fashion.

The political nature of the CIs

Most of the world's states support projects to promote their languages and cultures in one form or another. Comparisons of the CIs with organisations like the British Council, however, are misleading. In the first place, this is because the CIs have a primarily political agenda. Although this is not stated on the website of Hanban (Chinese National Office for Teaching Chinese as a Foreign Language) or in the contracts it signs with host institutions, Chinese leaders describe it as an organisation for spreading propaganda and building soft power. This is invariably repeated in the writings of Chinese academics in Chinese language journals on the topic. While the British Council does engage in political projects, such as the institutional development of justice, the rule of law and civil society, this is publicly stated on its website. Moreover, this cannot present a problem for foreign universities, because it does not establish offices on campuses.

Unlike the British Council, whose charter ensures that it is free from political interference, the CIs are closely linked to the Chinese Party-state. This can be seen in the first place in the way that the Hanban is affiliated with the Ministry of Education, an organisation that works according to a higher education law that is designed to uphold the ideological orthodoxy of "Marxism-Leninism, Mao Zedong Thought and Deng Xiaoping Theory". Moreover, the executive board and board of trustees of the British Council are composed of figures drawn either from the Council itself or from the worlds of the arts, business and commerce; the deputy director of the Hanban, however, is its CCP secretary and three of the sixteen members of its governing Council are members of the CCP Central Committee. The director, Liu Yandong, is a member of the Politburo and was head of the United Front Department from 2002 to 2003. Another member, Hu Zhanfan, has been president of China Central Television (CCTV) since 2011 and Chinese netizens have criticised him for telling journalists that they should understand that they are "propaganda workers". Given the importance of presenting the claim to sovereignty over Taiwan in China's foreign policy, it is also worth noting the presence of Zhou Mingwei on the Council, who has served as a deputy director of China's Taiwan Affairs Office and was dispatched to Washington in 2001 to lobby against arms sales to Taipei and any departure from the "one China principle".

Risks to universities

The first risk for host universities posed by CIs is that their political mission and links with the Chinese Party-state are not compatible with the principle of independence from political interference that is important for independent academic activity to flourish. This can be seen in the way in which the contract with the Hanban stipulates that the activities of CIs "shall not contravene...the laws and regulations of China". Moreover, signing the contract subjects all parties to the by-laws of the Confucius Institutes, which gives the Hanban the power to assess and adjudicate the performance of CIs. The Hanban is even empowered to invoke punitive consequences on any person or party who engages in "Any activity conducted under the name of the Confucius Institutes without permission or authorisation from the Confucius Institute Headquarters".[63]

This legal arrangement is more than an issue of abstract debate. The prejudicial nature of the Hanban's terms of employment, for example, has already become the focus of controversy and legal action. There is no secret about those terms, given that the Hanban's web site states that, to be considered for a teaching post, an individual must be "aged between 22 to 60, physical and mental healthy (sic), no record of participation in Falun Gong and other illegal organisations and no criminal record".[64] This situation has already led on employee of a CI in Canada, at McMaster University, to seek political asylum on grounds of religious persecution. By February 2013 the university had decided to resolve the issue by not renewing its contract with the Hanban. As well as posing a threat to the rights of individual employees, accusations that a university is supporting activities that are "unethical and illegal in the free world" can also pose a risk to the reputation of a university.

This reputational risk is compounded by the perception that CIs do not allow critical discussion of topics that the Chinese government deems sensitive, such as the status of Tibet and Taiwan or the 1989 Tiananmen massacre. This can be compounded when academics from China who have a record of promoting their government's policy are prompted to talk about such issues. Such was the case when pro-Tibet groups dismissed the CI at Sydney University as "a very good outlet for Chinese propaganda" in August 2012, for example, for organising a lecture by an academic from the Chinese Center for Tibetan Studies who has publicly stated that his mission is to explain to foreigners that Tibet has always been governed by China and has been rescued by the CCP from a scheme by the Dalai Lama to restore "a dictatorship of monks and aristocrats", and who links the self-immolations in Tibet to "overseas plots".

Again, such cases show that ethical standards are important to universities not just as a matter of abstract debate. They are important to protect and cultivate the secure environment that is necessary to promote the freedom of thought and expression upon which academic work depends. To grasp this point it is only necessary to put oneself in the position of an individual student or academic who is involved in or working on an issue the Chinese government deems sensitive. It is particularly disturbing when Chinese students express their fears and disappointment when they arrive at a university only to discover that their own government has established an organisation on campus that makes it feel as though they are still under the kind of surveillance with which they had to live in China. As one such student expressed it in a private email to the author, "The Confucius Institute, to me, functions like the closed circulation (sic) television and has the potential to scare away my critical thinking by constantly reminding me: we are watching you and behave yourself".

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Such feelings of insecurity are made worse by concerns that the Chinese government is engaged in collecting intelligence about the activities of individuals and the networks that many academics develop to further their research. It is not necessary to provide evidence that the CIs have been directly engaged in such activities when there is widespread evidence to indicate that the state for which they operate sponsors cyber-espionage on a grand scale against commercial and media organisations around the world. Although there is no direct evidence to prove a link between the Chinese state and hacking attacks on universities, it is significant that staff and research students doing work on China tend to be the targets of hacking. In spring 2010, for example, the London School of Economics and Political Science detected attempts to use tailored trojans to penetrate the email accounts of most of the staff and several research students working on issues related to Chinese politics and foreign policy. Multiple attempts had been made against seven targets. The top two scorers, who were working on issues deemed especially sensitive by the Chinese government, had been targeted no less than 59 and 28 times respectively.

As well as such immediate risks to universities, concerns have also been growing in the academic community that the CIs may distort the long-term development of Chinese studies. Particularly sensitive is the Hanban's insistence that CIs can only use the standardised form of Putonghua Chinese and the new, simplified form of Chinese characters. This has political implications because it denies students the opportunity to learn dialects such as Cantonese and the full-form, traditional characters favoured in the Chinese-speaking world beyond the control of the CCP, such as in Taiwan, Hong Kong and amongst the Chinese overseas. As Michael Churchman of the Australian National University explains, the directive that prevents foreigners from writing certain kinds of Chinese characters is based on the same underlying principle of encouraging them to extend their knowledge of China in ways acceptable to the Chinese state as the directive "You must not discuss the Dalai Lama". The result could be a generation of China scholars who will only feel comfortable working with a simplified version of China and will have difficulty dealing with historical texts or using media outlets that are critical of the CCP.

In a similar vein, towering figures in the field of sinology, such as Yu Yingshi, emeritus professor of East Asian studies and history at Princeton University, and Goran Malmqvist, professor of sinology at Stockholm University, have expressed their fears that reliance on CIs will encourage universities and governments to scale down funding for existing centres of expertise and specialist libraries and deny job opportunities to scholars trained outside China. Such a trend can also lead to the marginalisation of academics who refuse to work with CIs in their own institutions as they are denied access to contacts and the making of decisions that shape the relationship of their institution with China, not to mention the additional funds that universities have to contribute. Such a situation can lead to the growth of self-censorship and can even result in the departure of established academics, who would rather resign than see their own projects and organisations starved of funds and suffer the humiliation of decisions affecting their work being made over their heads. New members of the profession are in an even more vulnerable situation, especially if they have to commit themselves to working with a CI that is highlighted in job advertisements as a flagship project of the university.

When assessing the above risks, it should be borne in mind that the first CI concept was only established nine years ago and that the current plan is to expand the total number to 1,000 by 2020. A degree of mission creep can already be seen, going back to the establishment of the CI at Waseda University, in Japan in April 2007, in a partnership with Peking University that includes a program to assist the research activities of graduate students studying in China. CIs have also been broadening their work into projects such as holding discussions on topics such as China's financial system, its knowledge economy, its economic situation and the "China model".

When the Hanban held its annual conference in December 2012, it was felt that this "integration" (*rongru*) into the mainstream activities of universities abroad was too slow. A "new sinology plan" was thus announced, which aims to promote the involvement of CIs with the projects of doctoral students, youth leadership, study trips for scholars to "understand China", international conferences and assistance for publishing research. This is to be accompanied by greater efforts to penetrate the broader academic system of the host country by holding Chinese classes in junior and middle schools and by designing the local curriculum and by training a "brigade" (*duiwu*) of expert teachers.

Yet again, there are serious political implications of the CIs taking over the role of teacher training and curriculum design that are normally steered by academics trained in native universities. Controversy has already arisen over the political nature of the teaching materials provided to schools by the Hanban; This includes a lesson on the Hanban web site that described the Korean War as "The War to Resist US Aggression and Aid Korea". While older students may be better equipped to see through such attempts at indoctrination, Chinese academics are already drawing some satisfaction from evidence that American children who have studied under the direction of CIs have developed a more positive view of China and its political system.

Managing the risks

Many of those who defend the presence of the CIs on campus argue that they have not been exposed to political pressures. However, the political mission of the CIs, the unusual legal position they have staked out, the way in which they are perceived by vulnerable students and staff, the scale and speed of their development and the determination of the Hanban to expand their work into core academic activities and school education poses risks that need to be properly assessed and managed.

So far there has been only minimal discussion of whether the CIs can be managed within limits that are compatible with the mission of the university. It is interesting to note, however, a number of cases where the decision to host a CI has been actively resisted by academic staff on ethical grounds when put under proper scrutiny, most notably at the universities of Manitoba, British Columbia, Melbourne, Stockholm, Chicago and Pennsylvania.

The economic argument also needs to be set out more clearly, taking into account the matching funds, accommodation and administrative support provided by host institutions to CIs. When these are factored in, it may well be the case that it is more effective to train language teachers in-house, who will develop long-term careers, be familiar with local teaching methods and be free from political constraints. This would also open up opportunities for Chinese nationals who might be excluded under the Hanban system on political, religious or health grounds.

It is somewhat ironic that while many of the people who are most concerned about the risks posed by the CIs have spent their working lives devoted to Chinese studies, they are characterised by spokespersons for the Chinese government as purveyors of "Cold War thinking". Nobody can deny that there will and should be more academic engagement with China. All sides will benefit, however, if this is done in ways that are compatible with the mission of the university to uphold core values such as the pursuit of academic and intellectual freedom and respect for religious and political diversity. An alternative is to remove such values from the mission of the university. If the university is understood as an institution that not only reflects but also shapes the values of the society in which it is embedded, such a departure cannot be allowed to occur by default.

Age-old Temptations and the Protection of Trade Secrets

Chinese use of perception management

Although a diverse and complex country, China's overall grand strategy appears to have three inter-related goals: controlling its periphery, preserving domestic order and stability, as well as attaining and maintaining great-power status.

Perception management is an effective tool used by the country against perceived adversaries. Sun Tzu specifically called for such measures in his oft-quoted adage: "Deception is the way of military affairs". The Chinese government practices deception and perception management today in order to protect its strategic interests while deterring conflict. "It is better to subdue the enemy without engaging it in battle", also wrote the military strategist.

As a result, Beijing relies at times on manipulating an adversary's cognitive processes and producing perceptions that directly benefit China. Beijing has long placed significant emphasis on propaganda, or the manipulation of information made available to the public. The Tiananmen incident of 1989 is a telling example, as barely anyone in China remembers it today or what sparked the conflict. Manipulation of history from the Great Leap Forward to the Cultural Revolution also provides examples of how deft the Communist Party is in managing the nation's, as well as the outside world's, view of what is and is not history. China's Ministry of Foreign Affairs (MFA) consistently denies the country's involvement in cyber attacks, noting it is against Chinese law. What is not said, however, is that it is only against Chinese law to hack into another's computer *inside China*.

The methods employed by Chinese "collectors" to steal intellectual property are as diverse as the collectors themselves. They include collection using (i) direct requests, solicitation and marketing services; (ii) acquisition of technologies and companies; (iii) targeting conferences or other open venues, scientific exchanges, exchange students; (iv) exploiting joint research and official visits; (v) gaining employment in high-tech and research firms; and (vi) targeting of travellers overseas. Chinese collectors increasingly make use of technologically sophisticated methodologies such as cyber-attacks, the insertion of Trojan horse software, and the use of an "insider" within a company that often obfuscates China's hand and its goals.

Cases of theft of intellectual property in the United States

Lest there be anyone who questions whether foreign governments continue to involve themselves in stealing US technology, the following provides several examples.

(i) First there is the case of **Greg Chung Dongfan**[65], an engineer for Boeing and Rockwell, who passed restricted information on the space shuttle, the Delta IV rocket and the C-17 military cargo jet to China from 1979-2006 after becoming a naturalised US citizen. Chung's motive was to "contribute to the motherland". Initially, he travelled to China pretending to give lectures while secretly meeting with Chinese government officials and agents. He was also encouraged by his Chinese handlers to use Chi Mak (see below) to transfer information back to China. Chung was arrested in February 2008 and convicted in February 2010 of economic espionage and sentenced to over fifteen years in prison.

(ii) **Chi Mak** (Mai Dazhi) was a classic sleeper agent.[66] In March 2008, Chi Mak, a China-born, naturalised (1985) US citizen, was sentenced to over twenty-four years in prison. Chi Mak admitted he was sent to the United States in 1978 in order to obtain employment in the defense industry with the goal of stealing defense secrets, which he did for over twenty years.

He had been lead project engineer on a research project involving Quiet Electric Drive (QED) propulsion for use on US Navy submarines. The technology developed in the QED program is considered by the Navy to be Significant Military Equipment and therefore banned from export to countries specifically denied by the State Department, including China.

Beginning in 1983, Chi Mak passed this and other information to the PRC. In the early years, he and his wife transported the material to China, but after his brother Tai Mak arrived from China, he became the courier. Tai Mak encrypted the information and made arrangements to travel with the encrypted CDs to the PRC. Chi Mak admitted that the information he gave his brother was passed to a research fellow with the Chinese Center for Asia Pacific Studies (CAPS) at Zhongshan University in Guangzhou. CAPS is partially funded by, and conducts operational research for, the PLA.

(iii) In yet another case of espionage, a federal judge in Chicago on 29 August 2012, sentenced **Jin Hanjuan**, a Chinese-born, naturalised American, to four years for stealing millions of dollars in trade secrets from Motorola, describing the soft-spoken, unassuming woman as having carried out a "very purposeful raid" on the company in the dead of night.[67] Jin worked for Motorola from 1998 to 2007. Federal authorities stopped her during a random search at O'Hare International Airport in February 2007. She had a one-way ticket to Beijing. Customs agents discovered over US$30,000 in her luggage, as well as more than 1,000 confidential technical documents, that included paper copies, thumb drives, and information on several hard drives. A later search of her home found evidence that Jin had consulted on projects for Kai Sun News Technology Company, also known as Sun Kaisens, which is affiliated with China's military, since 2004 and emails indicated she intended to return to China to work for the company.

The judge in this case said "it was important to send a message that would deter others with access to trade secrets from siphoning off vital information. In today's world, the most valuable thing that anyone has is technology, hence the need to protect trade secrets."

(iv) Finally, on 29 May 2012, **Zhang Bo**, a Chinese citizen who worked for a contractor at the Federal Reserve Bank of New York, pleaded guilty to stealing US Treasury Department software used to track federal collections and payments. Zhang pleaded guilty to one count of theft of government property and one count of immigration fraud in a hearing in Manhattan federal court. On 4 December 2012,[68] Zhang was sentenced to six months of home confinement as part of a sentence of three years of supervised release. The judge in ruling on the case said there was no evidence that Zhang shared the computer code with anyone else or compromised the security of the software, but the judge was troubled by Zhang's continuing acts of illegal conduct. Zhang also admitted to submitting false documents to immigration authorities on more than one occasion to help foreign nationals obtain visas to enter and work in the US.

Zhang, a computer programmer formerly with Goldman Sachs, has been assigned to work on source code development at the New York Federal Reserve that related to the tracking of billions of dollars that are electronically transferred every day in the US general ledger. Zhang took advantage of the access that came with his trusted position to steal highly sensitive proprietary software. Stealing it and copying it threatened the security of vitally important source code. His case highlights what security experts call the "insider threat"—an employee working inside a company who steals intellectual property.

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6. The globalisation of Chinese interests has also resulted in an increased number of Party-state bureaucratic entities that are stakeholders in Chinese foreign affairs and national security policy.

7. The PRC rarely discusses LSGs in the public domain; neither the names nor numbers of these groups or their membership is published. Analysts believe the PLA has membership on the Foreign Affairs Leading Small Group (two seats: Defense Minister and Deputy Chief of the General Staff for Foreign Affairs and Intelligence); the National Security Affairs Leading Small Group (two seats: same as foreign affairs—these two organs are thought to be identical); the Taiwan Affairs Leading Small Group (two seats: the CMC Vice-Chairman responsible for operation's and the DCoGS or Foreign Affairs and Intelligence); and possibly a small group whose name is roughly the Politics and Law Committee (one seat for the Deputy Director of the PLA General Political Department, and one for the Commander of the People's Armed Police). The name and existence of this latter group is very tentative.

8. The constrained role of the PLA in domestic affairs is believed by some analysts to be the result of conscious decisions made by Deng Xiaoping in his final years in power. The last uniformed PLA officer to sit on the Politburo Standing Committee was Deng's life-long associate in the PLA, Admiral Liu Huaqing, who stepped down 1997.

9. It still remains unknown whether these PLA officers are acting on their own, whether they are fronting for a group of like-minded PLA officers or others, or whether their public activities are sanctioned.

10. In the mid- and late-1990s there were attempts to create such a coordinating mechanism modelled somewhat on the US National Security Staff. For reasons that are still not clear this never took place, although some analysts believe that

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